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August 6, 2013

Office of Regulations & Interpretations  
EBSA Room N-5655  
US Department of Labor  
200 Constitution Ave, NW  
Washington, DC 20210

Attn: Benefits Statement Project

RE: RIN 1210-AB20

Dear Ladies and Gentlemen:

As the Director of the Pension Research Council and Boettner Center at the Wharton School of the University of Pennsylvania, the oldest pension research group in the United States, I am pleased to respond to your Request for Information regarding the Benefits Statement Project. My responses are based on over 30 years of research and consulting in the retirement security arena; my views are my own and draw on research cited at the end of the attached memo.

The Administration is to be commended for working to help participants in defined contribution plans estimate the income amounts they might be able to receive from their pension plan accruals, taking into account the risk of longevity. My comments are intended to be helpful in the further development of the retirement calculator tool.

Thank you for your kind consideration. If you need additional information, please contact me at [mitchelo@wharton.upenn.edu](mailto:mitchelo@wharton.upenn.edu) or at 215 898 0424.

Sincerely yours,

A handwritten signature in cursive script that reads "OS Mitchell".

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*Submitted August 7, 2013*

*Response to the US DOL's Request for Public Comment on Proposed Rulemaking Regarding Pension Benefit Statements for Defined Contribution Plans (RIN 1210-AB20)*

Dr. Olivia S. Mitchell, The Wharton School, University of Pennsylvania

Plan participants in defined contribution plans could use help over their working lives and at retirement, to help them minimize or eliminate the risk of outliving their assets. Well-crafted retirement benefit calculators can be a useful and convenient tool for participants seeking to determine roughly how much income they could generate from a given amount of retirement savings. The calculator can help boost participant awareness of the chances of living a very long time by illustrating how important it is to cover “tail” survival risk instead of focusing on life expectancy during the retirement payout phase. Such a tool will particularly benefit the financially less literate, who are least likely to understand the implications of survival to very old ages.

The DOL's calculator is a sensible first step on the path to building a more useful and more complete tool that could actually be used by employees deciding how much to save and what to draw down during retirement. The calculator could be maintained by DOL and recommended by plan sponsors who would encourage workers to access it at various points in their careers, so the employees could decide if they were more or less “on track” building their retirement incomes. Of course a disclaimer would be needed by both the government and plan sponsors, to the effect of “exact results may vary.”

What would be most helpful is to provide users a sense of the possible annual income benefits from their current account balances, as well as projected to the Social Security normal retirement age. I would also find it useful to have an option whereby the user of the tool could enter in his/her spouse's age (if any). The resulting computations would permit participants to gain a clearer idea of the potential retirement income streams that could be derived from their retirement accounts, taking into account longevity risk.

If the calculator could be made a bit more interactive, this would also help. Some possible interactions might include:

- I do favor showing the user several amounts: the immediate payout amount given current accruals, the projected benefit given current accruals, and the projected benefit assuming contributions continue to a future date (e.g. the normal retirement age under Social Security). Each estimate would of course need to be caveated with a statement that contributions and benefits are not guaranteed.

- I also suggest that the calculator present all results in *real terms*, so that the relationship between wage growth, investment returns, etc. is comparable in today's dollars. Most people won't understand what future dollars can buy them, or the complicated interrelationships between the many terms and assumptions (such as, for instance, that an inflation rate of X implies a nominal return of Y).<sup>1</sup>
- Related to this is that, after retirement, benefits are usually fixed in nominal terms (so they decline in real terms). To get people to think about this, the tool could give the user two choices for the payout illustrations: one would preserve purchasing power of today's dollars (i.e. a real annuity), and the other would decline at (say) 3% per year, equivalent to a fixed nominal annuity with 3% inflation.
- It would be helpful if the calculator could be used to run experiments where the participant boosted the amount of earnings saved, to see how this would alter the payout amount.
- I would give the user more choice over projected investment returns. The low could be the return on TIPS, and the high maybe the 7% you propose now (though I am uneasy about that in the context of life cycle funds).
- You can readily permit the user to add a spouse/partner (and that person's age) and recomputed the benefit, if desired.
- I would recommend you allow the user to specify an expected income tax rate post-retirement, so the calculator will generate spendable (rather than gross) income (give the user some low/middle choices).
- Assuming zero loads is clearly too conservative; a better approach would be to provide the user a choice of loads over a reasonable range of investment options (industry bottom and top quartile). Otherwise people could be misled regarding what they are likely to find in the market if they seek an annuity.
- It should probably be disclosed that the payouts will be likely higher for men if they buy an annuity outside the qualified plan as they will get the single sex mortality table pricing; conversely for women.
- It would also be useful to have a caveat to users, that if they do not annuitize the lump sums but instead keep investing them, they could withdraw about a third less per year in an effort to save enough to avoid running out of money.

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<sup>1</sup> In this context, I believe that assuming a 3% real earnings growth rate is high; one could instead let the user select his own assumption (from a range of -5 to +5, say).



### **Related research:**

Brown, Jeffrey R., Arie Kapteyn, & Olivia S. Mitchell. (*forthcoming*). “Framing and Claiming: How Information-Framing Affects Expected Social Security Claiming Behavior.” *Journal of Risk and Insurance*. (NBER WP 17018.)

Chai, Jingjing, Wolfram Horneff, Raimond Maurer, and Olivia S. Mitchell. (2011). “Optimal Portfolio Choice over the Life Cycle with Flexible Work, Endogenous Retirement, and Lifetime Payouts.” *Review of Finance*. 15(4): 875-907.

Horneff, Wolfram, Raimond Maurer, Olivia S. Mitchell, and Ivica Dus. (2007). “Following the Rules: Integrating Asset Allocation and Annuitization in Retirement Portfolios.” *Insurance: Mathematics and Economics*. 42: 396-408.

Horneff, Wolfram, Raimond Maurer, Olivia S. Mitchell, and Michael Stamos. (2009). “Asset Allocation and Location over the Life Cycle with Survival-Contingent Payouts.” *Journal of Banking and Finance*. 33(9): 1688-1699.

Lusardi, Annamaria and Olivia S. Mitchell. (*forthcoming*). The Economic Importance of Financial Literacy: Theory and Evidence.” *Journal of Economic Literature*. (NBER WP 18952),

Maurer, Raimond, Olivia S. Mitchell, Ralph Rogalla, & Vasily Kartashov. (*forthcoming*). “Lifecycle Portfolio Choice with Stochastic and Systematic Longevity Risk, and Variable Investment-Linked Deferred Annuities.” *Journal of Risk and Insurance*. (NBER WP 17505)

Mitchell, Olivia S. (2011). “Managing Risks in Defined Contribution Plans: What Does the Future Hold?” In *Growing Old: Paying for Retirement and Institutional Money Management After the Financial Crisis*. Eds. Yasuyuki Fuchita, Richard J. Herring and Robert E. Litan. Brookings Institution Press and Nomura Institute of Capital Markets Research: 75-94.

Mitchell, Olivia S. , John Piggott, & Noriyuke Takayama, eds. 2011. *Revisiting Retirement Payouts: Market Developments and Policy Issues*. Oxford: Oxford University Press.