The ESOP Association

Lifetime Income Disclosure Requirement

Background

All defined contribution plans, including employee stock ownership plans (ESOPs), must provide a benefit statement to each participant annually. Plans that allow participants to direct investments, like most 401(k) plans, must provide statements more frequently. This is a requirement under ERISA section 105, which also details the content that must be reflected on the benefit statement.

The SECURE Act of 2019 amended ERISA section 105 to require that a lifetime income disclosure be included in at least one benefit statement in a 12-month period for all defined contribution plans, including ESOPs.

The Department of Labor now requires disclosures that provide a set of assumptions to be used in computing the projected monthly payment amounts. These include an assumed interest rate and mortality assumptions. Use of these assumptions and the model disclosure limits any liability on the plan sponsor or plan fiduciary regarding the accuracy of the projections.

The purpose of this requirement is to help participants understand how the amount of money they have saved so far converts into an estimated monthly payment for the rest of their lives and how this impacts their retirement planning.

These requirements consist of:

- Projected monthly payment amounts a participant would receive if the total accrued benefit was used to provide a single life annuity or a joint and survivor annuity; and
- a model disclosure that explains the projections.

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What is an ESOP?

An Employee Stock Ownership Plan (ESOP) is a tax-qualified retirement plan authorized and encouraged by federal tax and pension laws. Unlike most retirement plans, ESOPs:

- Are required by law to invest primarily in the shares of stock of the sponsoring employer.
- Are trusts that hold shares of the business for employees, making them beneficial owners of the company that employs them.
- Can provide tax benefits to the company and to the exiting owner(s).
- Can borrow money from related parties to finance company projects—including the tax-advantaged purchase of the company's shares of stock.

Learn more about ESOPs at:
esopassociation.org/what-is-an-esop

Action Items

ESOP participants are confused by the annuity amounts and disclosure language. Reforms should be made for ESOPs and similar organizations that allow plan sponsor or plan fiduciary to more clearly communicate that the disclosure requirement is a federal mandate that does not reflect the value of the ESOP nor the amount the participant can expect to receive upon retirement.

POINT OF CONTACT

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Issues Related to ESOPs

- ESOPs are generally funded entirely with employer contributions and the primary investment is company stock.
- Participants cannot impact the employer provided benefit levels in the ESOP; they have no ability "to save more" in an ESOP.
- Participants do not have the ability to direct investments in the ESOP.
- ESOPs benefits are not paid out as annuities; they are paid in single sums or installments.
- The reflection of possible annuity income may be discouraging or confusing to the ESOP participants; they cannot change the employer contribution and they may already have adjusted their 401(k) savings to the maximum possible.

What ESOP companies are experiencing

- Participants are confused by the annuity amounts and the disclosure language.
- It has a negative impact on new participants who have not had time to build their ESOP balance yet; amounts are small and discouraging.
- This distracts from the meaningfulness of the employer benefit levels provided by the ESOP.
- This is not resulting in participants wanting to know how to save more.