GAO Highlights

Highlights of GAO-15-74, a report to the Ranking Member, Committee on Ways and Means, House of Representatives

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PRIVATE PENSIONS

Participants Need Better Information When Offered Lump Sums That Replace Their Lifetime Benefits

Why GAO Did This Study

Since 2012, a number of large pension plan sponsors have given selected participants a limited-time option of receiving their retirement benefits in the form of a lump sum. Although sponsors' decisions to make certain lump sum "window" offers may be permissible by law, questions have been raised about participants' understanding of the financial tradeoffs associated with their choice. GAO was asked to review critical issues associated with these types of offers.

This report focuses on 1) the prevalence of lump sum offers and sponsors' incentives to use them, 2) the implications for participants, and 3) the extent to which selected lump sum materials provided to participants include key information. To conduct this work, GAO identified sponsors offering lump sum windows and used social media to identify participants given offers. GAO reviewed 11 informational packets acquired through interviews with selected plan sponsors and participants. GAO also analyzed lump sum calculations and interviewed federal officials and pension experts.

What GAO Recommends

GAO recommends that DOL improve oversight by requiring plan sponsors to notify the agency when they implement lump sum windows, and coordinate with Treasury to clarify guidance on the information sponsors provide to participants. Further, Treasury should reassess regulations governing relative value statements, as well as the interest rates and mortality tables used in calculating lump sums. Agencies generally agreed with GAO's recommendations.

View GAO-15-74. For more information, contact Charles Jeszeck at (202) 512-7215 or jeszeckc@gao.gov.

What GAO Found

Little public data are available to assess the extent to which sponsors of defined benefit plans are offering participants immediate lump sums to replace their lifetime annuities, but certain laws and regulations provide incentives for use of this practice. Although the U.S. Department of Labor (DOL) has primary responsibility for overseeing pension sponsors' reporting requirements, it does not require sponsors to report such lump sum offers, making oversight difficult. Pension experts generally agree that there has been a recent increase in these types of offers. By reviewing the limited public information that is available, GAO identified 22 plan sponsors who had offered lump sum windows in 2012, involving approximately 498,000 participants and resulting in lump sum payouts totaling more than $9.25 billion. Most of these payouts went to participants who had separated from employment and were not yet retired, but some went to retirees already receiving pension benefits. Sponsors are currently afforded enhanced financial incentives to make these offers by certain laws and regulations issued by the U.S. Department of the Treasury (specifically the Internal Revenue Service) governing the interest rates and mortality tables used to calculate lump sums.

Participants potentially face a reduction in their retirement assets when they accept a lump sum offer. The amount of the lump sum payment may be less than what it would cost in the retail market to replace the plan's benefit because the mortality and interest rates used by retail market insurers are different from the rates used by sponsors, particularly when calculating lump sums for younger participants and women. Participants who assume management of their lump sum payment gain control of their assets but also face potential investment challenges. In addition, some participants may not continue to save their lump sum payment for retirement but instead may spend some or all of it.

GAO reviewed 11 packets of informational materials provided by sponsors offering lump sums to as many as 248,000 participants and found that the packets consistently lacked key information needed to make an informed decision or were otherwise unclear. Using various sources, including financial advisors, federal agency publications, laws, and regulations, GAO identified eight key types of information that participants need to have a sound understanding of a lump sum offer. While GAO did not review the packets for compliance or legal adequacy, most packets provided a substantial amount of this key information. However, all of the packets GAO reviewed lacked at least some key information. For example, the relative value notices were often unclear about how the value of the lump sum compared to the value of the lifetime monthly benefit provided by the plan. Similarly, many packets did not clearly indicate the interest rate or mortality assumptions used, limiting participants' ability to assess how the lump sum payment was calculated. Further, few of the packets informed participants about the benefit protections they would keep by staying in their employer's plan—full or partial protections provided by the Pension Benefit Guaranty Corporation, the agency that insures defined benefit pensions when a sponsor defaults. This omission is notable because many participants GAO interviewed cited fear of sponsor default as an important factor in choosing the lump sum.