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August 7, 2013

Office of Regulations and Interpretations
Employee Benefits Security Administration
Room N-5655
U.S. Department of Labor
200 Constitution Avenue, NW
Washington, DC 20210
Attention: Pension Benefit Statements Project

Re: Advanced Notice of Proposed Rulemaking Regarding Pension Benefit Statements
[RIN 1210-AB20]

Dear Sir or Madam:

On behalf of our members, the Insured Retirement Institute (“IRI”) ¹ appreciates the opportunity to provide comments in response to the Department of Labor’s (“DOL”) request for comments on the Advanced Notice of Proposed Rulemaking regarding Pension Benefit Statements (RIN 1210-AB20) (the “Notice”). We commend DOL for its continued focus on the promotion of guaranteed lifetime income products and strategies. This is a great first step in DOL’s initiative to facilitate greater availability and use of these products, and to increase participant understanding of guaranteed lifetime income. We look forward to working with DOL on this rulemaking, and urge DOL to continue pursuing other regulatory efforts in furtherance of this critically important endeavor, including proposals to address the other issues raised in IRI’s response² to the joint DOL and Treasury Department’s Request for Information Regarding Lifetime Income Options for Participants and Beneficiaries in Retirement Plans (the “Lifetime Income RFI”).

¹ The Insured Retirement Institute has been called the “primary trade association for annuities” by U.S. News and World Report. Our official mission is to: (1) encourage industry adherence to highest ethical principles; (2) promote better understanding of the insured retirement value proposition; (3) develop and promote best practice standards to improve value delivery; and (4) advocate before public policy makers on critical issues affecting insured retirement strategies.

² Available on DOL’s Web Site at www.dol.gov/ebsa/pdf/1210-AB33-615.pdf.

IRI is the only national trade association that represents the entire supply chain for the insured retirement strategies industry. We have over 500 member companies, including major insurance companies, broker-dealers, banks, and asset management companies. Our member companies represent more than 97% of annuity assets, and include the top 15 distributors ranked by assets under management. Our members are represented by more than 150,000 registered financial advisors who serve clients in multiple states and communities across the country, and therefore, IRI brings together the views of Main Street America and the annuities industry. From this perspective, we respectfully offer the following comments.

Executive Summary

1. We strongly support the concept of providing lifetime income illustrations on participant benefit statements.
2. We strongly support DOL's decision to call for lifetime income illustrations in the form of annuities because annuities are the only financial instruments available today that can guarantee a lifetime stream of income throughout retirement.
3. In deciding whether to require illustrations based on participants' current account balances and/or projected account balances, DOL should determine the information that will have the greatest impact on retirement savings behavior.
4. We are concerned that including specific assumptions in the safe harbors described in the Notice will steer plan sponsors to utilize those assumptions to ensure compliance at the expense of flexibility and innovation.
5. In lieu of the safe harbor approach, we urge DOL to adopt a rule under which plan sponsors would be required to provide lifetime income illustrations based on generally accepted investment theories and generally accepted actuarial principles.
6. We urge DOL to include in the rule a clear statement that providing the illustrations required under the rule would be treated as education, and not as a fiduciary act giving rise to either fiduciary or plan liability.
7. We recommend that DOL allow plan sponsors the flexibility to provide reasonable disclosure about lifetime income illustrations, and have developed draft disclosure language that DOL could provide for plan sponsors to use (on an optional basis) to help ensure that providing the required illustrations will not be considered a fiduciary act.
8. We believe there are valid reasons why different plan sponsors might prefer to use different ages to calculate lifetime income illustrations, and therefore, recommend that DOL allow plan sponsors the flexibility to determine what retirement age to use.
9. We believe there are valid reasons why certain plan sponsors might prefer not to use the terms of annuities actually offered by their plans to calculate such illustrations, and therefore,

recommend that DOL allow plan sponsors the flexibility to determine whether to use such terms rather than generally accepted investment theories and generally accepted actuarial principles.

10. We recommend that DOL require illustrations at least annually, but also provide flexibility for plan sponsors to determine whether to provide illustrations more frequently based on relevant factors such as cost and the needs of their plan participants.

Background – Workers Need Guaranteed Lifetime Income

Seventy-nine million Baby Boomers today face immediate and unprecedented retirement income challenges—challenges that simply did not exist in earlier generations. Between 2000 and 2010, the number of 60-64 year old Americans has increased by more than 50%, from 10.5 million to more than 16.2 million. According to the Mortality Tables from the Society of Actuaries,³ a 65-year-old male has a 30 percent chance of living to age 90, and a 65-year-old female has a 42 percent chance. A couple age 65, has a 60 percent chance of one or both being alive at 90, and a 30 percent chance that one or both will live to 95. Simply put, individuals today are living longer than their parents and grandparents, and therefore must take a much longer-term approach to planning and saving in order to support themselves through retirements that can span 20-30 years or more.

As the population in the United States ages and more Boomers retire or approach retirement, concerns about financial preparedness remain high. The combination of longer life spans and a declining birth rate mean the ratio of workers to retirees will continue to decline, increasing pressure on public and private pensions systems, and health care systems. In addition, Baby Boomers and Generation Xers bear more of the risk and responsibility for retirement savings and income production than prior generations. An ever-increasing number of companies are transitioning from traditional pension plans to defined contribution plans such as 401(k)s, meaning that much of the burden for retirement security has been transferred from employers to individuals. Employees have to make decisions about whether to participate in a 401(k) plan, how much to save, and how to invest. And at retirement, participants have to figure out how to make their nest egg last for life – while managing the risks that go along with that.

The Employee Benefits Research Institute's 2012 Retirement Readiness Ratings⁴ reveal the result of this transition. Nearly half of all Baby Boomers – over 35 million Americans –and almost 45% of Generation X (ages 36-45) are “at risk” for inadequate retirement income, not having sufficient guaranteed lifetime income.

Despite this sobering fact, IRI research has shown that Boomers who own insured retirement products, including all types of annuities, have greater confidence in their overall retirement expectations, and are more likely to engage in positive retirement planning behaviors than those who do not. Nine out of ten

³ UP94, a pensioner mortality table with full projections from the Society of Actuaries, with analysis by Ron Gebhardtshauer, Faculty-in-Charge, Actuarial Science Program, Smeal College of Business, Penn State University.

⁴ Employee Benefits Research Institute. “Retirement Income Adequacy for Boomers and Gen Xers: Evidence from the 2012 EBRI Retirement Security Projection Model.” (May 2012)

Boomers who own annuities believe they are doing a good job preparing financially for retirement, 73 percent believe that annuities are a critical part of their retirement strategy, 68 percent have calculated a retirement goal, and 63 percent have consulted with a financial advisor.

And because annuities help address numerous risks retirees face, including longevity risk and inflation risk, financial advisors and Boomers are increasingly seeing the need for the guaranteed lifetime income provided by annuities, particularly middle-income families who make up the bulk of annuity owners. Our survey of financial advisors revealed that 84 percent are having more retirement-income discussions with clients, and 71 percent had a client request to purchase an annuity during the last year.

Annuities⁵ are the only financial instruments available today, other than Social Security and pensions, that guarantee a lifetime stream of income throughout retirement. With the proper use of annuity products and other retirement savings vehicles, retirees can be assured they will not outlive their assets and benefit significantly by having the ability to maximize their income in retirement.

Earlier this year, IRI released a report on the results of a study⁶ that pinpoints guaranteed lifetime income options offered within employer-provided defined contribution plans as an opportunity to address many emerging retirement security challenges. The study, a copy of which is attached as Appendix A to this letter, found that workers who convert a portion of their accumulated assets into a guaranteed income stream can effectively manage many of the risks inherent to the defined contribution retirement system such as longevity risk, volatility and sequence of returns risk, as well as excess withdrawal risk.

With an increasing amount of consumers agreeing that annuities are a critical component of a retirement strategy, there is a growing appetite for these types of options. In fact, nine in 10 workers would like for their plan sponsor to offer an income-generating option within their retirement plan. Clearly, there is a tremendous opportunity here for the DOL, the insured retirement industry and plan sponsors to work together to make guaranteed lifetime income options more accessible.

Support for Lifetime Income Illustrations Requirement⁷

Given the need to educate workers about their lifetime income needs, we strongly support the concept of providing lifetime income illustrations on participant benefit statements. Many plan participants see the lump sums in their retirement accounts as sufficient to cover their expenses and support their

⁵ IRI members offer a variety of guaranteed lifetime income solutions. Some of these solutions may not be treated as annuities for tax purposes, but nonetheless offer lifetime income guarantees. For purposes of this comment letter the term “annuity” should be read as including all guaranteed lifetime income products.

⁶ Insured Retirement Institute. “Guaranteed Lifetime Income Options within Employment-Based Plans.” (January 2013). <http://www.myirionline.org/docs/default-source/default-document-library/in-plan-options.pdf?sfvrsn=0>

⁷ For purposes of this comment letter, we use the terms ‘projection’ and ‘projected account balance’ to refer to a participant’s estimated account balance based on future earnings and/or contributions, and the terms ‘illustration’ and ‘lifetime income illustration’ to refer to the estimated monthly income amount that would be generated by either the participant’s current or projected account balance.

desired lifestyle during retirement. Unfortunately, for most people, this perception is flawed because they do not understand how to properly assess the actual value of the amount they have been able to save. Lifetime income illustrations would go a long way towards helping participants put their savings in the proper perspective, spur them to begin saving more, and enable them to budget and plan more effectively.

Moreover, we strongly support DOL's decision to call for lifetime income illustrations in the form of annuities. This approach is consistent with DOL's interest in promoting access to guaranteed lifetime income. While other products and strategies can and should play a valuable role in the development of holistic retirement plans, it is wholly appropriate for DOL to use an annuity structure as the basis for conversion in this context, given that annuities are the only products that guarantee income throughout retirement.

In the pages that follow, we will provide specific comments and suggestions to improve the effectiveness of the draft rule included in the Notice (the "draft rule").

Input on Use of Current or Projected Account Balances

Consistent with the comments DOL received in response to the Lifetime Income RFI, our member companies have differing opinions about whether DOL should include the requirement for illustrations based on projections. Given these divergent views, IRI is not taking a position on this question. Rather, we will provide an overview of the thoughts raised by our members with respect to both approaches.⁸

Our member companies who support the inclusion of projections have argued that doing so provides an important and helpful context for the illustration based on the current account balance. Without this, providing illustrations based only on the current account balance could discourage participants from maintaining or increasing their savings rates. For participants with low account balances, seeing just how little monthly income their accounts would generate could make the effort appear futile. Furthermore, those member companies have observed that projections can offset potential distortion resulting from market volatility and short-term market swings. Since illustrations are, by their nature, tied to a specific point in time, using only current account balances creates the risk that the illustration will be generated at an unusually high or low point.

In addition, member companies supporting projections question the utility of illustrations based solely on the participant's current account balance, and believe that illustrations based on projected future contributions and earnings are more realistic. Given that participants will contribute additional amounts and experience investment gains over time, these companies believe such future contributions and gains should be included in the projection. In sum, they feel that illustrations based only on the static

⁸ While we do not have a consensus among our members as to whether projections should be required, this letter does include several comments that address various issues involving projections. These comments should not be read as supporting or opposing the concept of including projections; rather, these comments are intended only to provide feedback to DOL in the event it decides to proceed with a rule that would require projections.

current account balance would not achieve the DOL's goal of encouraging participants to think in terms of future lifetime income and plan appropriately.

By contrast, other member companies are concerned that including illustrations based on both current and projected account balances would be confusing and/or overwhelming for many participants. These companies believe that too much information would lead to inaction, which would obviously be counterproductive if the primary goal is to encourage positive changes to savings behavior. In this regard, our members are concerned that the required illustrations, explanations and caveats are not being disclosed in isolation, but rather as part of a broader individual benefit statement, with respect to which regulations have yet to be issued. For this reason, a number of our members are concerned that adding further information and complexity will only serve to discourage more participants from reviewing their individual benefit disclosures. In addition, these companies are concerned that the additional costs and burdens associated with developing and implementing the systems changes will not only impact providers, but also small and midsize employers who are becoming increasingly concerned about costs and fiduciary liability, especially in light of the new participant fee disclosure requirements.

If DOL determines that participants should receive projected account balances and illustrations based on such projections, these member companies believe such information would be more effectively conveyed through the use of online tools and calculators, which can be tailored to more accurately reflect the individual participant's financial situation. This approach would give participants access to additional information that could help ensure they are on the right path in terms of retirement saving and planning without rendering benefit statements needlessly long and complex.

Ultimately, IRI believes DOL must determine what information will have the greatest impact on retirement savings behavior, without overwhelming or discouraging participants from considering the illustrated amount(s) or the benefit statement generally. The approach DOL ultimately decides to propose must ensure that the intended benefits have a reasonable prospect of success and can be achieved in a cost effective manner.

Methodology and Assumptions

We appreciate DOL's effort to provide a safe harbor that provides assumptions plan sponsors can use to comply with the draft rule's requirement that projections and illustrations be based on "reasonable assumptions." We are concerned, however, that this approach will steer plan sponsors to utilize the safe harbor assumptions to ensure compliance at the expense of flexibility and innovation. Projections and illustrations based on the safe harbor assumptions may be reasonable and appropriate, but more meaningful and individualized tools are currently available in the marketplace, usually on the Internet, but the safe harbor approach would likely discourage plan sponsors from making such tools available to their participants. In lieu of the safe harbor approach, DOL should simply require that plan sponsors provide lifetime income illustrations based on account generally accepted investment theories and generally accepted actuarial principles. In this regard, we note that the industry has developed a standardized methodology for calculating annuitization rates, which plan sponsors should be permitted (but not necessarily required) to utilize. In the Notice, DOL already recognizes that illustrations meeting

this standard would be acceptable as long as participants have access to the underlying assumptions and receive the requisite disclosures (which we will specifically address below). Furthermore, we urge DOL to include in the rule a clear statement that providing the illustrations required under the rule would be treated as education, and not as a fiduciary act giving rise to either fiduciary or plan liability.

If DOL ultimately decides to move forward with a rule that includes fixed assumptions similar to those included in the draft rule, the rule should also expressly provide that lifetime income illustrations based on generally accepted investment theories and actuarial principles would be treated as education and not as a fiduciary act (as described above), such that plan sponsors could use the DOL-provided assumptions as an alternative for participant benefit statements while enabling sponsors to direct participants to more detailed complementary resources. In such case, we offer the following general suggestions to help guide the formulation of such assumptions:

- Such assumptions should be very basic and simple. DOL should resist any temptation or recommendation to build more complexity into the assumptions in an effort to create more accurate illustrations or projections. It is important that DOL keep in mind that the goal is to provide information to incentivize behavioral changes, not to provide precise predictions of future outcomes.
- With respect to the assumption regarding the use of mortality tables, we would encourage DOL to require the use of mortality rates for healthy individuals, since that would generate the most conservative illustrations. Using less conservative assumptions might over-inflate the estimated monthly income that could be generated by participants' account balances (whether current or projected), which might result in participants not saving enough for retirement. Moreover, participants likely would not realize that they have under-saved until they have little or no time left to save more.

If DOL determines to include assumptions in any proposed rule, we may have additional comments or suggestions with respect to the details of those assumptions.

Recommendations Regarding Disclosures and Explanations

While it is important to develop appropriate rules regarding the content of illustrations and projections, in several ways, it is even more critical that the rules adequately address the need for accurate and meaningful disclosures and explanations. Clearly, this is essential for plan sponsors, who need clear guidance as to exactly what they must do to satisfy their obligations under ERISA. From the perspective of plan participants, the effectiveness of illustrations and projections to meet DOL's goal of enhancing retirement savings will depend heavily on the quality and clarity of the disclosures and explanations that accompany the numbers on the benefit statement.

The disclosure provisions in the draft rule cover some of the key points already, such as the fact that illustrations are not guarantees and could vary based on a variety of factors. In addition, we believe DOL should allow plan sponsors to provide additional information (i.e., education) about their illustrations and projections, such as steps participants can take to get their retirement savings back on track,

warning language about the potential impact of market volatility, and access to on-line calculators and other tools and resources that participants can use to generate more personalized illustrations and projections.

Based on these points, we are providing draft disclosure language that DOL could provide for plan sponsors to use to help ensure that providing the required illustrations will not be considered a fiduciary act. To be clear, we believe plan sponsors should have the flexibility to provide reasonable disclosure that meets the minimum requirements included in the draft rule. We are not proposing that all plan sponsors be required to use this (or any other) exact language.

For illustrations based only on current account balances:

“The lifetime income stream illustration provided on this statement is intended only to help you understand how your current account value could translate into monthly income in retirement. It is not guaranteed by, and does not constitute investment advice from, your employer, your retirement plan, any service provider to the plan, or any other person or company. It is only an estimate based on certain assumptions, including the assumptions listed below. This illustration does not reflect any possible future contributions or earnings. It is also based solely on market conditions on the date of this statement, and could therefore be impacted by market volatility and short-term market swings. Your actual monthly retirement income will depend on numerous factors and will vary from this illustration.

To see how this illustration might change if different assumptions were used, please visit [website address] or call [telephone number].

For more information about retirement planning and savings, please visit [website address] or call [telephone number].

You should consult with a financial professional to understand how to read and use this illustration.”

For illustrations based on both current and projected account balances:

“The projected account balance and the lifetime income stream illustrations provided on this statement are intended only to help you understand how your current account value could grow over time and how your current and projected account balances could translate into monthly income in retirement. They are not guaranteed by, and do not constitute investment advice from, your employer, your retirement plan, any service provider to the plan, or any other person or company. They are only estimates based on certain assumptions, including the assumptions listed below. They are also based solely on market conditions on the date of this statement, and could therefore be impacted by market volatility and short-term market swings. Your actual future account balance and your actual monthly retirement income will depend on numerous factors and will vary from this projection.

To see how the projection and illustrations might change if different assumptions were used, please visit [website address] or call [telephone number].

For more information about retirement planning and savings, please visit [website address] or call [telephone number].

You should consult with a financial professional to understand how to read and use this illustration.”

Retirement Age

We understand why DOL chose to use normal retirement age, but there are a number of reasons that plans should be permitted to use other ages. First, requiring a specific age may cause administrative costs and complications to plan sponsors and service providers, and confusion to participants, given that some plans have different normal retirement ages. Further, there are valid reasons to use other ages for this purpose. For example, some participants will find it more useful to base illustrations and projections (if provided) on the Social Security retirement age, as this would enable them to assess their sources of guaranteed retirement income as of a single age, and would therefore facilitate (and encourage) more holistic retirement planning in conjunction with the social security benefit statement. Alternatively, because the vast majority of plans have a normal retirement age of 65 and many individuals think of age 65 as their target retirement age, plan sponsors should be permitted to tie illustrations and projections (if provided) to that age.

Ultimately, as in other matters discussed herein, we believe the rule should provide flexibility for plan sponsors to decide how to meet their obligations under ERISA, and tailor the retirement age selected to the needs and characteristics of the qualified plan and its participants. Of course, the illustration should clearly specify the age of reference for illustrations and projections (if provided). In this context, specifically, we think such flexibility would provide meaningful benefits, and would help avoid potential confusion for participants.

Use of Terms of In-Plan Annuities

While we recognize the logic in requiring that illustrations be based on the terms of products actually offered by a plan, we do not believe this would be universally appropriate or advisable. A particular plan sponsor may have numerous reasons to prefer to present illustrations based on more generic assumptions, even if the plan actually offers an annuity product. For example, a plan could offer multiple annuities with different terms or the plan sponsor might decide to change the investment options and/or forms of distribution offered through their plan. In either case, using a specific product could add significant cost and complexity (with minimal corresponding benefit) in calculating illustrations. Accordingly, we believe all plan sponsors should have the option to provide illustrations that are based on “reasonable assumptions”. Sponsors who are comfortable providing illustrations based on the terms of annuity products actually offered in their plans should have that option, but we do not believe it should be mandatory.

Frequency of Illustrations

We encourage DOL to afford plan sponsors the flexibility, taking into account the relevant costs and the needs of their plan participants, to determine how frequently illustrations should be provided. Our member companies have observed that certain plan sponsors might prefer to provide illustrations quarterly, so that participants get updated information with every benefit statement, while other sponsors might believe this would be more data than their participants would want. Similarly, depending on the size of the plan, it might be more or less cost effective for different plans to provide illustrations more or less frequently. Nevertheless, we recommend that DOL require illustrations at least annually, thereby ensuring all participants receive an illustration at least once a year.

Joint and Survivor Illustrations

Our member companies have expressed concerns about the requirement in the draft rule that plan sponsors provide married participants with illustrations based on joint and survivor (J&S) annuities. In many cases, recordkeepers do not have enough information to know whether the J&S rules apply (e.g., marital status, existence of QDRO). Accordingly, we believe it would be better to provide all participants with illustrations based on individual annuities, and include information about where married participants can learn more about J&S annuities.

DOL Authority

We note that the Notice points to Sections 105(a) and 505 of ERISA as providing the statutory authority for the draft rule. Under Section 105(a), administrators of DC plans must provide participants with periodic benefit statements, including the “total benefits accrued”, at least annually (quarterly if the plan permits participants to direct their own investments). In addition, Section 109(c) of ERISA provides DOL may prescribe the format and content of any report, statement or document that is required to be provided to plan participants and beneficiaries. IRI believes Sections 105 and 109(c) provide DOL with sufficient authority to require lifetime income illustrations as part of individual benefit statements.⁹

Conclusion

We are grateful for the opportunity to present our members’ views on the Notice. In moving forward with this rulemaking, we encourage DOL to remain cognizant of the fact that the goal is not to provide precise or near-precise predictions of future results; rather, the goal is to motivate participants to start saving more so that they will be more likely to achieve their retirement goals. Precise illustrations are not needed to achieve this important objective.

We commend DOL for advancing this very important initiative, and we look forward to working with DOL to develop a rule that meets the laudable goals expressed in the Notice without imposing undue burdens or creating needless fiduciary liability risks for plan sponsors. We also urge DOL to continue

⁹ We are expressing no view with respect to DOL’s authority under section 505 of ERISA.

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working on other regulatory efforts as part of its ongoing initiative to increase participants' access to and utilization of guaranteed lifetime income products, including proposals to address the other issues raised in IRI's response to the Lifetime Income RFI.

Please feel free to contact me, Lee Covington, Senior Vice President & General Counsel (202-469-3002) or Jason Berkowitz, Vice President of Regulatory Affairs & Compliance (202-469-3014), if we can provide additional information or to further discuss these issues.

Sincerely,



Catherine J. Weatherford
President & CEO

Appendix A



Insured Retirement Institute

Guaranteed Lifetime Income Options within Employment-Based Plans

Leveraging Advantages and Overcoming Challenges

January 2013

About the Insured Retirement Institute: The Insured Retirement Institute (IRI) is a not-for-profit organization that for more than twenty years has been a mainstay of service, commitment and collaboration within the insured retirement industry. Today, IRI is considered to be the authoritative source of all things pertaining to annuities, insured retirement strategies and retirement planning. IRI proudly leads a national consumer education coalition of nearly twenty organizations and is the only association that represents the entire supply chain of insured retirement strategies: Our members are the major insurers, asset managers, broker-dealers/distributors, and 150,000 financial professionals. IRI exists to vigorously promote consumer confidence in the value and viability of insured retirement strategies, bringing together the interests of the industry, financial advisors and consumers under one umbrella. IRI's mission is to: encourage industry adherence to highest ethical principles; promote better understanding of the insured retirement value proposition; develop and promote best practice standards to improve value delivery; and advocate before public policymakers on critical issues affecting insured retirement strategies and the consumers that rely on their guarantees. Visit www.IRIONline.org today to experience the vast resources of the Insured Retirement Institute for yourself.

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The issue of income in retirement is upon us now. Baby Boomers started becoming eligible for Social Security benefits in 2008, the year the first Boomers turned 62. In 2011, 44% of individuals who first claimed Social Security benefits did so at age 62. As employers have shifted from defined benefits plans, which provided guaranteed lifetime income in retirement, to defined contribution plans, which typically pay out a retirement benefit in a lump sum, the responsibility for managing assets in retirement is now with individuals.

As a result, individuals must now identify strategies and solutions to help effectively manage the multiple risks that may arise in retirement. Guaranteed income products such as annuities can help individuals better manage these risks. Previous IRI research has identified some of the risks that guaranteed products could help manage, including longevity risk, market risk, excess withdrawal risk, asset allocation risk, sequence of withdrawal risk, and incapacity risk.

A way to help individuals who are saving for their retirement through a defined contribution plan to manage these risks is by providing a mechanism within the plan through which they have the option to convert a portion of their accumulated assets into a guaranteed income product. This report will examine the following points:

- Individuals are not well prepared to manage their income in retirement on their own.
- Including guaranteed income options within employment-based defined contribution plans as a consideration for retirement planning.
- Advantages of providing guaranteed income options through employment-based defined contribution plans for both employees and employers.
- Challenges around providing guaranteed income options through employment-based defined contribution plans.

Key Findings

- Providing guaranteed income options within an employment-based plan is appealing to plan participants. According to one study, 89% of participants agree they would like their plan sponsor to provide them with income-generating options in their retirement plan.
- Retirement products that include guaranteed income features can help Americans ensure they have sufficient income in retirement. IRI research shows Boomers value guarantees and the value of those guarantees increases with age. Among Boomers age 60 to 66, 19% stated the most important trait of a retirement product is guaranteed income each month compared with 14% of Boomers age 50 to 54.
- Advantages to plan participants of in-plan guaranteed income options:
 - Protection against market volatility close to retirement
 - Access to ongoing employer-provided financial education on guarantee options
 - Lower fees through group purchasing
- Advantages to employers of in-plan guaranteed income options:
 - Increased utility of the defined contribution plan as a labor force management tool assisting employees to retire when planned
 - Increased participant satisfaction and confidence, leading to better participant outcomes.
- Challenges providing in-plan guaranteed income options

- Fiduciary concerns are the most significant obstacle to increased offering of guaranteed lifetime income options.
- Current low take-up rates
- Flexibility of product offerings
- Portability of products
- Concerns regarding giving up control over retirement assets
- Evidence from IRI’s research on Boomers shows few Boomers are very to extremely knowledgeable about investing in securities.
- Results from the National Financial Capability Study indicate relatively low levels of financial literacy.
- Research from IRI and Cogent Research shows annuity owners are increasingly more likely to agree that annuities are a critical part of a retirement strategy, increasing by 18 percentage points from 55% in 2011 to 73% in 2012.

Are Individuals Prepared to Manage Their Assets in Retirement?

One way to assess whether Americans are financially prepared for retirement is to determine their level of financial knowledge. In 2009, in consultation with the U.S. Department of the Treasury and the President's Advisory Council on Financial Capability, the FINRA Investor Education Foundation commissioned a national study of the financial capability of American adults. In this study, individuals were exposed to a battery of questions covering fundamental concepts of economics and finance expressed in everyday life. The questions involved calculations involving interest rates and inflation, principles relating to risk and diversification, the relationship between bond prices and interest rates, and the impact that a shorter term can have on total interest payments over the life of a mortgage. The results, illustrated in the table below, indicate relatively low levels of financial knowledge.

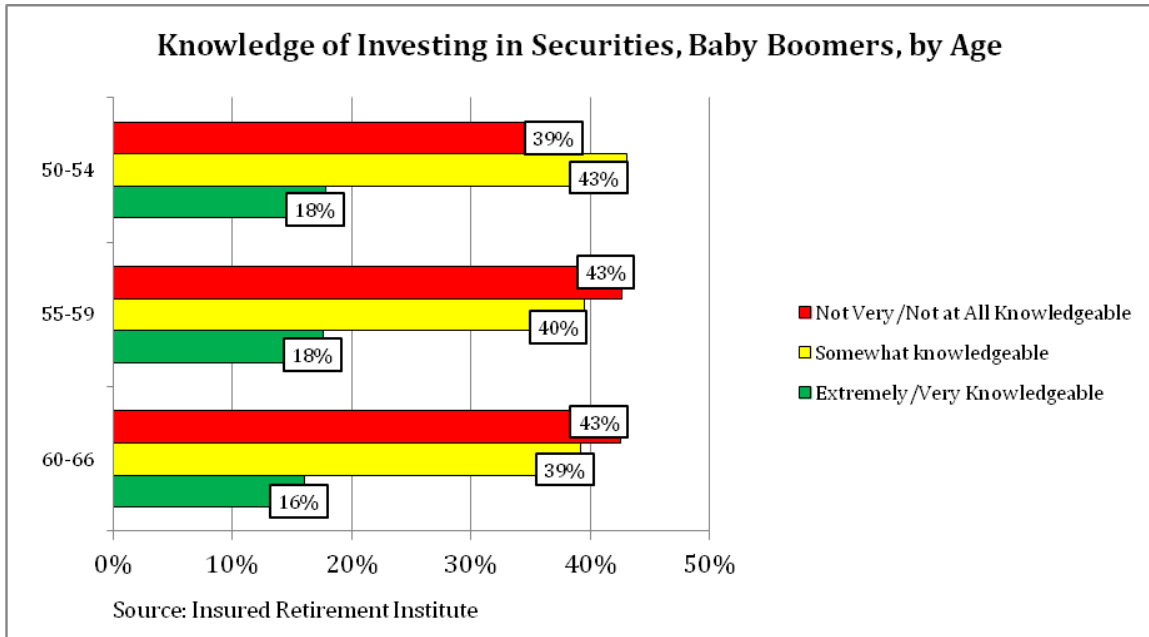
Measures of Financial Literacy

	Correct	Incorrect	Don't Know
Interest Rate Question	65%	21%	13%
Inflation Question	64%	20%	14%
Bond Price Question	21%	44%	34%
Mortgage Question	70%	16%	12%
Risk and Diversification Question	52%	13%	34%

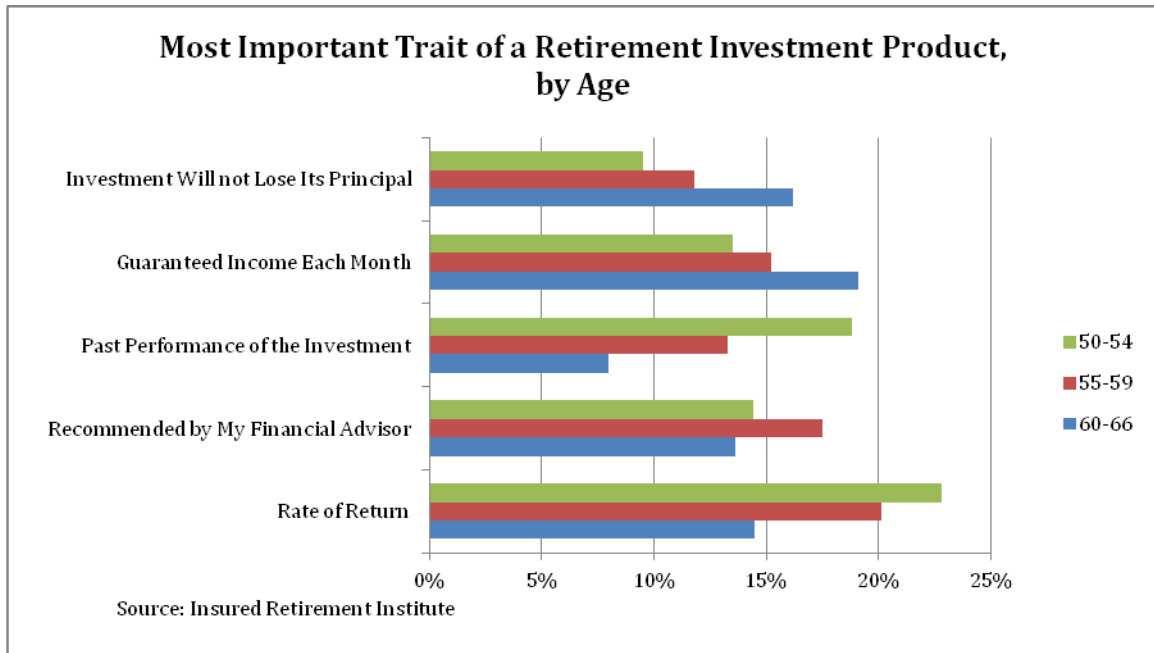
Source: FINRA Investor Education Foundation

While the correct response to any single question sometimes exceeded 60 percent, fewer than half of respondents (46 percent) correctly answered both a question about interest rates and a question about inflation. Less than one-third (30 percent) correctly answered those questions plus a question about risk and diversification correctly. Fewer than 10 % of respondents were able to answer all questions correctly.

In order for individuals to be able to manage their retirement assets on their own throughout their retirement, which could be longer than twenty years, knowledge of investing in products such as securities would be helpful. Yet, IRI research shows most Boomers, among all age groups analyzed, lack knowledge on investing in securities. A large majority of Boomers, a little over 80% in all age categories, reported they are somewhat to not at all knowledgeable of investing in securities. While less than one-fifth of Boomers report they were very to extremely knowledgeable about investing in securities.



The evidence from these two studies demonstrates that most Americans lack the financial skills necessary to manage their assets in their retirement years. As a result, retirement products that include guaranteed income features could play an important role in the retirement plans of most Americans. IRI has found through their research on Boomers that these guaranteed income features are highly valued. In fact, the value Boomers place on these features increases with age as they approach retirement. For example, among Boomers age 60 to 66, 19% stated the most important trait of a retirement product is guaranteed income each month compared with 14% of Boomers age 50 to 54. Research conducted by IRI and Cogent Research demonstrates that current owners of annuities highly value these products as a part of their retirement strategy. In their joint study, *Evolution of the Annuity Industry™ 2012*, 73% of annuity owners strongly or somewhat agreed with the statement, "I believe annuities are a critical part of a retirement strategy." This is an increase of 18 percentage points from 2011.



While these products will be components in the retirement income planning process, Americans will need assistance in making the retirement financial decisions appropriate for them. An avenue to provide some assistance lays with providing guaranteed income solutions within employment-based defined contribution plans such as 401(k)s.

Advantages of Guaranteed Income Options Within Defined Contribution Plans

Advantages to Employees

Offering guaranteed lifetime income options through employment-based defined contribution plans has many advantages for individuals. There is a strong connection between saving for retirement and work. For many Americans, the primary vehicle for saving for their retirement is through an employment-based plan. According to the Bureau of Labor Statistics, in 2012 68% of all workers in private industry and state and local governments had access to a retirement savings plan through their employer. Even for non-employment-based plans such as IRAs, the majority of dollars added to IRAs comes from employment-based plans. According to the Employee Benefit Research Institute, in 2010 almost twelve times more dollars were added to IRAs through rollovers from an employment-based plan than from direct contributions.

Given this strong connection between retirement savings and the workplace, many plan participants want their employer to provide in-plan options. According to BlackRock's *Annual Retirement Survey: What Retirees Have to Tell Us About the New World of Retirement*, 89% of participants agree they would like their plan sponsor to provide them with income generating options in their retirement plan and 85% find the idea of a fund that automatically converts savings to guaranteed income in retirement appealing. Purchasing guaranteed income products through the employer's plan provides participants with lower costs due to group purchasing. Participants also benefit from the screening process employers use in selecting service providers for their plans. However, this creates challenges for employers with regard to their fiduciary liability. Further discussion of this issue follows in the challenges section of this report.

Protection Against Market Volatility Close to Retirement

The protection available with annuities is particularly valuable in protecting plan participants during the several years before and after their retirement date. During this time, market volatility can be especially harmful to retirees because they have less time to recover and a larger asset base at risk. Market volatility can also cause income volatility when income is based on assets held in the market. It can also markedly increase the probability of outliving one's assets, especially if a downturn occurs early in retirement. Annuities with their guaranteed income distribution options can help stabilize at least part of a retiree's income and can provide longevity protection.

Benefits of Employer-Provided Education

The need for education on income needs in retirement is essential. The employer is a trusted source of financial education. Employers and service providers currently are providing financial education on the topic of saving for retirement. Adding in education on managing those assets in retirement can be seen as the next step. Employees will benefit from ongoing education on the value of guaranteed income options. Specifically, within an employment-based plan, participant education materials should clearly and concisely explain the benefits of guaranteed lifetime income products and how they compare to other options that are offered by their plan. This would include information such as the historic return patterns of each of the options, the specific risk ratios associated with each of the plan choices, the expense ratios or fees associated with each option, and an explanation of differences between and among different options. Similar educational information is already provided in the accumulation stage under the plans. However, this creates challenges for employers with regard to their fiduciary liability. Further discussion of this issue follows in the challenges section of this report.

The education efforts should present guaranteed income products as a component of an individual's plan for providing income in retirement, not as the only solution. Many elderly individuals have loss aversion when it comes to their finances and may see giving up control of their assets for a guaranteed income product as a form of financial loss. See the section *Concerns Regarding Giving Up Control Over Retirement Assets* for further detail on this topic.

Moreover, while it is clear that, at a minimum, participants should receive educational materials on lifetime income options as they near retirement and the distribution stage, it would also be prudent to provide extensive information earlier in a participant's career with the employer. This would ensure that participants would be able to formulate an appropriate long-term retirement plan.

A simple first step is to require benefit statements that include the annuity equivalent of a participant's benefit. This was the goal of the Lifetime Income Disclosure Act of 2011. When individuals receive their benefit statements today, they see their benefit expressed as a single lump sum amount. That naturally leads them to think of their 401(k) plan benefit as a lump sum amount, not as a source of guaranteed income for life. This can have a subtle but powerful effect on their decision regarding how to receive their 401(k) plan benefit. It is critical that participants be made more aware of the possibility of receiving at least a portion of their benefit in an annuity form that protects them against outliving their savings. Knowing the amount of monthly income they can expect will help employees evaluate whether they are on the path to retirement security.

In this regard, benefit statements that provide annuity equivalents would be better coordinated with Social Security benefit statements, which only express benefits in the form of a life annuity. Individuals would be able to determine the total retirement income available to them during their retirement. Thus, the proposal would build on the success of Social Security benefit statements, providing additional information regarding retirement income.

Advantages to Employers

One of the advantages of a defined benefit plan to employers is the plan's utility as a labor force management tool. When an employer needs to downsize the workforce for economic or business reasons, the employer could use early retirement options within the defined benefit plan. Some of the advantages of downsizing the labor force through early retirement incentives are: It is less disruptive to remaining works and retired employees remain connected to the employer, allowing the possibility to incent former workers with key skills back into employment if a need arose.

Prudential found in *The Future of Retirement and Employee Benefits: Finance Executives Share Their Perspectives* that a large percentage of respondents in the 2012 survey (69%) say they believe a significant number of their companies' employees will be forced to delay retirement due to inadequate savings. Delayed retirements can limit companies' abilities to hire new staff and provide advancement opportunities for existing talent. Respondents also frequently predict that delayed employee retirements would affect their company's ability to control workforce costs (44%). As a result, some employers are considering ways to enhance their defined contribution plans to assist employees to retire when planned. Among the options being considered are guaranteed lifetime income products, indicated by 41% of respondents.

In a separate study, *Better Participant Outcomes Through In-Plan Guaranteed Retirement Income*, Prudential found, when in-plan guaranteed retirement income options are added to defined contribution plans:

- Participant satisfaction increases,
- Participant confidence increases, and
- Participant outcomes improve due to better long-term investing behaviors.

In addition, the research found that plan participants with in-plan guaranteed retirement income options were more inclined to stay invested during market turmoil, were better diversified, and contributed more than participants without guaranteed retirement income.

Challenges to In-Plan Guaranteed Income Options

In addition to the advantages to in-plan guarantee options, there are challenges that need to be overcome. The following gives a brief overview of some of those challenges.

Fiduciary Liability

Fiduciary concerns are the most significant obstacle to increased offering of guaranteed lifetime income options. The Department of Labor (DOL) has adopted rules meant to help employers understand what they must do to satisfy their fiduciary obligations when choosing to offer an annuity option in their plans. Unfortunately, these rules include a broad, vague requirement that employers conduct a detailed review of an insurer's financial condition and conclude that insurer will be able to meet all of its long-term commitments. These commitments are significant given the nature of the insurer's liability in the

participant's lifetime. This is a task for which most employers are not well equipped and is fraught with legal liabilities. Therefore, this presents a serious deterrent for a plan sponsor.

With regard to participant education, plan sponsors are concerned that any attempt to educate participants about these products and provide relevant information could create potential fiduciary liability, either because the information might be deemed "investment advice" under Employee Retirement Income Security Act (ERISA), or because any deficiency in such information could constitute inadequate disclosure and/or misrepresentation about a plan product or feature. The DOL could address these concerns by amending its existing regulatory materials on this subject (including Interpretive Bulletin 96-1, Field Assistance Bulletin 2007-1) or by issuing new guidance to clarify that plan sponsors can provide information about lifetime income products to assist their participants in evaluating available alternatives, whether inside or outside of the plan, and that providing such information will not give rise to any potential fiduciary liability.

The DOL could help plan sponsors by clarifying that they will not face fiduciary liability for providing educational materials to their plan participants. The DOL should develop and distribute a model disclosure that would accompany an illustration of the product and therefore mitigate the fiduciary responsibility of the plan sponsor.

When promulgating the qualified default investment alternative (QDIA) regulations, some in the industry asked the DOL to include stable value products (such as fixed products that include guaranteed annuity purchase rates) as one of the options that could be used as the QDIA, and the DOL declined to do so. This issue should be revisited because QDIAs are important safe harbors that plan sponsors rely on. The fact that there is a guaranteed feature should not disqualify these products from being QDIAs. It may require some additional disclosure to participants to ensure they understand the fee structures associated with these products.

Low Take-Up Rates for Current Guaranteed Products

The issue of low take-up rates can be resolved through participant education on the value of these products. However, much of the current education is on the accumulation phase of saving, and little attention has been paid to the decumulation phase. Prudential found in *Better Participant Outcomes Through In-Plan Guaranteed Retirement Income* that nearly half of those who had not invested in an in-plan guaranteed retirement income option said it was simply because they were unaware one was available. Once participants were informed, perceptions about and interest in guaranteed retirement income was considerable. Guidance is needed in the area of participant education, especially if plan sponsors and providers are being asked to increase their education efforts about distribution, including lifetime income options.

Framing of the allocation options within the plan can have significant impacts on outcomes. A metastudy by Allianz, *Behavioral Finances and the Post-Retirement Crisis*, found in a study by Jeffrey Brown from the University of Illinois that positioning guaranteed income products as income solutions dramatically increases their attractiveness.

Flexibility of Product Offerings

A disadvantage for participants in selecting an in-plan guaranteed lifetime income option could be flexibility, if the product offered in-plan lacks features that a participant could choose in the open market. Options that address inflation, death benefits, and liquidity

concerns might not be available in the in-plan option. However, the plan sponsor can avoid this situation by choosing products with these features. In addition, more than one type of guaranteed product could be offered.

Portability of Products

Lifetime income products contain special costs for their guaranteed features, and it is assumed that the product will remain in the plan until the participant can elect the guaranteed feature, thereby getting the benefit of what he or she paid for. However, due to service provider changes and merger and acquisition activity, that product might not remain as an option for the plan participants. The portability of guaranteed lifetime income products is a big concern for plan sponsors, and the IRA rollover rules currently do not offer a clear solution. These issues are of particular concern to small employers, who do not have negotiating power to cause a new vendor to make system changes necessary to support guaranteed lifetime income products. The Treasury Department may conclude that a solution would require a statutory change to various distribution provisions of the Internal Revenue Code affecting 401(k), 403(b), 457(b), and other plan types.

Concerns Regarding Giving Up Control Over Retirement Assets

An AARP and American Council of Life Insurers (ACLI) study *What Now? How Retirees Manage Their Money to Make It Last Through Retirement* found that retirees are very loss adverse. Given this loss aversion, it seems intuitive that retirees would prefer guaranteed products. However, the study found the retirees who were more loss adverse were not as open to annuitized income solutions as the less loss averse. Allianz in *Behavioral Finances and the Post-Retirement Crisis* highlights findings by Prof. Eric Johnson at Columbia University that retirees view giving up control as a form of loss. Positioning guaranteed products as a way of gaining control over income and spending could help alleviate retirees' concerns over loss of control. Prof. David Laibson of Harvard University agrees positioning of annuities is important in getting participants to accept them. If you frame annuities as guaranteed income for life, investors are all for it, but the minute you frame it as a loss of control, they lose interest. Laibson believes investors will feel more secure about annuities if they are framed as a small piece of a very large portfolio. This is less threatening than putting all of their assets into one account with limited liquidity.

Conclusion

We are at the beginning of a long and complex debate. The question of how average Americans will manage their assets in retirement presents many complex issues to resolve. As demonstrated here using data from the FINRA Investor Education Foundation and IRI, individuals are not prepared to take on this task. Assistance is needed. The question of where that assistance will come from is still an open one. This report has explored the possibility of providing this assistance through employment-based defined contribution plans. While this option presents many advantages to participants, such as ease of transition of assets into guaranteed products, lower rates for fees, employer selection of service providers, and employer provided ongoing education, there are many challenges for employers. From the employer perspective, chief among these challenges are the fiduciary liability concerns regarding provider selection and the determination of whether information provided is education or advice.

The issues of an aging population, increased longevity, and the coming large wave of retiring Boomers means this debate is certain to have serious implications for American society for many decades to come.

Methodology

The Insured Retirement Institute (IRI) commissioned Woelfel Research, Inc., to conduct a survey of Boomers approaching retirement or who have recently retired. The research was conducted by means of telephone interviews with 803 adult Americans age 50 to 66. The sample was selected from a list of households in this age group, developed by Accudata, Inc., by compiling data from available sources such as motor vehicle records. Results were weighted by age and gender to the 2010 United States Census. Data were collected during February and March 2012.

Supporting data were derived from publicly available research from financial services companies (Allianz, BlackRock, and Prudential) and other organizations (AARP, American Council of Life Insurers, Cogent Research, Employee Benefit Research Institute, and FINRA Investor Education Foundation).