April 30, 2010

The Honorable Phyllis Borzi
Assistant Secretary, Employee Benefit
Security Administration
Department of Labor
Washington, DC 20210-0002

The Honorable J. Mark Iwry
Senior Advisor to the Secretary, Deputy Assistant
Secretary for Retirement and Health Benefits
Department of the Treasury
Washington, DC 20220-0002

Nancy J. Marks
Division Counsel/Associate Chief Counsel
Tax Exempt and Government Entities
Internal Revenue Service
Department of the Treasury
Washington, DC 20224-0002

RE: RIN 1210-AB33

The Committee on Investment of Employee Benefit Assets (CIEBA) is the voice of the Association for Financial Professional (AFP) on employee benefit plan asset management and investment issues. CIEBA is a nationally recognized forum for ERISA-governed corporate pension plan sponsors on fiduciary and investment matters. CIEBA represents 120 of the nation's largest retirement funds. Its members are the senior corporate financial officers who individually manage and administer corporate retirement plan assets. CIEBA members manage $1.1 trillion in defined benefit plan and defined contribution plan assets on behalf of 15 million participants.

CIEBA commends the Departments of Labor and Treasury and the Internal Revenue Service for issuing the *Request for Information Regarding Lifetime Income Options for Participants and Beneficiaries in Retirement Plans.* By seeking input from a wide spectrum of stakeholders, the agencies should benefit from information that will help identify ways to better assist retirement plan participants prepare for their retirement.

The following CIEBA submission was prepared by a group of CIEBA members with practical experience dealing with participants and plan investment issues. We did not respond to every question, including those that required special expertise, such as the actuarial and legal questions, or questions related to out-of-plan activities.

The following are some of the key points addressed in our submission:

- Lifetime income options are not yet widely available in defined contribution plans.
- Greater understanding of and access to appropriately structured lifetime income options would be beneficial to many participants.
- To date, participants have shown little interest in lifetime income, for a variety of reasons.
- Communications/education will be key in ‘moving the needle’ on participant interest in lifetime income options.
- Currently, there are significant barriers affecting plan sponsors’ ability and willingness to offer lifetime income options.
- More clarity around safe harbor provisions and guidelines are needed in a variety of areas, including counter-party risk and liability, communications, and reinsurance and structure of appropriate products.

If you need additional information, please contact CIEBA’s Managing Director Judy Schub at (301) 961.8682 or at jschub@afponline.org.

Sincerely,

Robert M. Hunkeler
Chairman
CIEBA

CIEBA Responses to RFI on Lifetime Income Options in Retirement Plans
(RIN 1210-AB33)
Submitted April 30, 2010

General

1. From the standpoint of plan participants, what are the advantages and disadvantages for participants of receiving some or all of their benefits in the form of lifetime payments?

Advantages:

- *Participants are less likely to outlive their income, thus providing protection against longevity risk.*
- *It is simple and predictable. Good for budgeting in retirement as it is a known income.*
- *Purchasing deferred products in advance of retirement assists participants with critical retirement savings decisions in the working years leading up to retirement.*
- *Removes the burden of appropriately managing and effectively drawing down their own assets. Most individuals are simply unable to do this effectively without some form of insurance or risk sharing.*
- *If participants receive some Lifetime income (as opposed to all), it becomes a diversifier.*
- *Reduces the risk of poor or of unscrupulous financial advice.*

Disadvantages:

- *Inflation may erode buying power in some product designs. Some product designs limit or eliminate the opportunity for growth in assets and/or income.*
- *Some product designs limit or eliminate the ability of a participant to access assets in an emergency or bequeath balances.*
- *Assets may not be portable to another provider or investment or portability may be very limited in comparison to common investment alternatives.*
- *Product expenses may include additional layers of fees in comparison to common investment alternatives which may erode buying power.*
- *There will always be individual winners (who live longer) and losers (who do not live as long). This may lead to adverse selection where participants who have health conditions that may shorten their life expectancy do not choose lifetime payments.*
- *Exposure to the risk of default or impairment of the annuity provider.*

2. Currently the vast majority of individuals who have the option of receiving a lump sum distribution or ad hoc periodic payments from their retirement plan or IRA choose to do so and do not select a lifetime income option. What explains the low usage rate of lifetime income arrangements?

- *Marketing by brokers, paid financial advisors and/or retail mutual funds:*
    - *Over-estimation of possible returns,*
    - *Under-estimation of investment risks and impact of fees, and or*
    - *Little or no recognition of longevity risk.*
- *Poor positioning or lack of in-plan options in Defined Contribution (DC) plans.*

- *Herding behavior tends to lead many participants away from considering a Lifetime income option. Individuals who do not know others who have utilized a Lifetime income option are less apt to utilize one themselves. Similar factors impact organizations sponsoring plans which defer the introduction of such options in part because peers do not offer similar options.*
- *Lack of transparency and knowledge of the factors which drive cost and benefits.*
- *A lack of education around Lifetime income products. Most individuals and organizations do not understand annuity-type investments. Even when information is available, most participants do not have the time or inclination to develop a practical understanding of the costs and benefits of these options in the absence of salient incentives.*
- *Individuals do not want to leave assets with a Defined Benefit (DB) plan and potentially be subject to bankruptcy/Pension Benefit Guaranty Corporation (PBGC) limits.*
- *More sophisticated individuals who may consider an institutional annuity do not want to be subject to the credit risk of an insurance company.*
- *Few individuals and organizations understand the operation of the "Safety Net" provided by state guaranty associations or how it varies from state to state.*
- *People tend to overestimate the amount of income which may be reliably generated by their wealth. They think the lump sum has a greater value than an equivalent annuity.*
- *People underestimate their lifespan and the number of years spent in retirement. Further, it is difficult for individuals to determine how much income they will need in retirement.*
- *People want to be able to bequeath assets to their heirs rather than insure income for their lifetime.*
- *People like to be in control of their assets and overestimate their investment expertise in managing their retirement savings.*
- *People tend to suffer from status quo bias. They become familiar with tracking their "balance" during their working years and consider that to be their end goal rather than the income it should generate in retirement.*
- *Participants are individuals with varying needs. Current retirees or those now nearing retirement may already have retirement income through a DB plan along with retirement savings in a DC plan.*
- *Small account balances may not cover the administrative cost of annuitization and may make the small monthly annuity generated unattractive and impractical.*
- *Participants might have an immediate financial need for their assets or worry about a future emergency need*

Is it the result of a market failure or other factors (e.g., cost, complexity of products, adverse selection, poor decision-making by consumers, desire for flexibility to respond to unexpected financial needs, counterparty risk of seller insolvency, etc.)?

- *Virtually all of the examples listed in the question contribute to current low utilization rates. However, some specific causes may contribute more than others:*
    - *Lack of financial literacy.*

- *Most current DC plan designs include an implicit default to lump sum payouts, since Lifetime Income options are not offered in most cases, or are an opt-in feature in the few cases where they are available. Research on participant behavior shows that most participants accept a default in the absence of incentives to do otherwise.*
- *The benefits and risks of various Lifetime Income options are often less obvious than the perceived benefits and risks of maintaining a large balance in an investment-only account.*
- *It is virtually impossible for most people to equate the present value of a stream of future payments to a single lump sum.*
- *Lack of unbiased reference points to judge the relative merits of a product. Decision makers (both participants and plan sponsors) would benefit from evaluating products in comparison with well designed and broadly available benchmarks. Few, if any, of these exist today.*
- *The decision to choose a Lifetime Income option is very complicated and unstructured. Individuals are generally unable to accurately gauge the risks or relative merits of such products without clear and simple guidance. There are few sources of such guidance available to participants or plan sponsors.*
- *In many cases, the decision to use a lifetime income option is irrevocable. Participants fear that their circumstances could change, making the decision to 'buy' a lifetime income option a bad decision.*
- *In the past and to some extent today, many defined contribution plan participants also receive an annuity from a defined benefit plan, reducing their need for additional lifetime income options.*

Are there steps that the Agencies could or should take to overcome at least some of the concerns that keep plan participants from requesting or electing lifetime income?

- *Promote tax advantages and/or other forms of incentives for Lifetime Income over other forms of distribution.*
- *Provide clear and robust guidance for plan sponsors with regard to the extent and nature of Safe Harbor provisions governing the selection of providers as well as the description and presentation of Lifetime Income options in retirement plans.*
- *Establish a central repository of unbiased and reliable educational material on which plan sponsors may rely for plan design decisions and which may be used to develop communications for or distribution to plan participants.*
- *Encourage plan sponsors and advice providers to offer advice that continues past the asset accumulation phase.*
- *Encourage partial annuitization in Defined Benefit plans that offer lump sums.*

3. What types of Lifetime Income are currently available to participants directly from plans (in plan options), such as payments from trust assets held under a defined benefit plan and annuity payments from insurance contracts held under a defined contribution or defined benefit plan?

- *Very limited offerings in most 401(k) plans.*

- *While some DC plans offer annuities or other guaranteed products, the take up rate by participants has been very low. Some plans have eliminated annuity features due to low or no usage.*
- *Some DC plans offer distribution programs which draw down assets based on a formula, fixed percentage of assets or fixed dollar amount where participants pick the amount, the frequency and the duration of the payments. Some plan sponsors report that this type of program is relatively popular. However, these programs do not guarantee that distributions will extend for the life of the participant, which participants may not fully understand.*
- *By law, all DB plans offer annuity options to participants. Many large pension plans do not allow lump sum distributions. For example, in 2008, more than 80 percent of the dollars paid out by CIEBA members' plans were recurring payments.*
- *However, when plans offer lump sums, a large percentage of participants opt for this form of benefit.*

4. To what extent are the Lifetime Income options referenced in question 3 provided at retirement or other termination of employment as opposed to being offered incrementally during the accumulation phase, as contributions are made? How are such incremental or accumulating annuity arrangements structured?

- *Some insurance companies offer an accumulation product in which participants can contribute throughout their working lives. These products provide dollar cost averaging into annuity amount.*
- *Newer guaranteed minimum withdrawal features allow contributions while active.*
- *Several designs being considered by the large plan market focus on establishing a floor on retirement income through the incremental or large-scale purchase of deferred payout products during a participant's working years.*
- *Most of these designs establish an annual amount of income which a participant may withdraw from their assets in retirement and guarantee that participants will continue to collect a minimum amount of income even after their assets are depleted.*
- *Various designs differentiate themselves in several respects, most importantly, the manner in which the amount of guaranteed income is determined, the manner in which the amount of guaranteed income may increase over the life of the participant, the level of fees paid by the participant leading up to and in retirement, and the structure of the guarantee itself.*
- *At least two broadly discussed designs further differentiate themselves from single insurer products by offering variations on a multi-insurer approach.*

5. To what extent are 401(k) and other defined contribution plan sponsors using employer matching contributions or employer non-elective contributions to fund Lifetime Income? To what extent are participants offered a choice regarding such use of employer contributions, including by default or otherwise?

- *At least one well publicized product design focuses on employer contributions as the funding source for the purchase of deferred Lifetime Income. However, as far as we know, this product has not been adopted by any plans as of this date.*

- *Virtually all of the existing products and designs currently under development in the large plan market may be adapted to use employer contributions as the primary source of funding. Behavioral finance research would suggest that designing default actions to include such contributions would lead to wider adoption among plan participants.*
- *Two issues that continue to discourage employer matching or non-elective contributions going to lifetime income options are:*
    - *Need for better safe harbors.*
    - *Need to address portability concerns raised by some lifetime income option products.*

6. What types of Lifetime Income or other arrangements designed to provide a stream of income after retirement are available to individuals who have already received distributions from their plans (out-of-plan options), such as IRA products, and how are such arrangements being structured (fixed, inflation adjusted, or other variable, immediate or deferred, etc.)? Are there annuity products under which plan accumulations can be rolled over to an individual retirement annuity of the same issuer to retain the annuity purchase rights that were available under the plan?

- *We do not know of any such arrangements.*

7. What product features have a significant impact on the cost of providing lifetime income or other arrangements designed to provide a stream of income after retirement, such as features that provide participants with the option of lifetime payments, while retaining the flexibility to accelerate distributions if needed?

- *The price of options are generally driven by the following factors:*
    - *Market conditions, especially volatility, impact cost of hedging,*
    - *The level and term structure of interest rates across the entire yield curve, but 10-year nominal Treasuries, in particular, and*
    - *Riskiness of underlying investments' asset allocation and the availability and cost of liquid hedging instruments to offset the risk of the underlying investment allocation (e.g., equity futures contracts and interest rate swaps).*
- *The most expensive features of a guaranteed product may change depending on the nature of other features included. For example, products which provide participants with the ability to withdraw all or a portion of their principal without penalty will increase the cost of the longevity option embedded in the product.*
- *One feature that was commonly offered prior to the financial crisis of 2007-2009, but subsequently withdrawn from virtually all products is known as a "roll up". Roll ups guarantee the participants that the asset base used to calculate their income benefits will increase by a minimum percentage each year. This form of guarantee became problematic during the financial crisis. Another feature which is sometimes confused with a roll up, but is far less expensive is known as a "ratchet". This feature continues to be offered in many products today. A ratchet provides the opportunity for income to increase, but only if certain values, such as the participant's current account balance, are higher than at a previous measurement date. This is sometimes referred to as a "High Watermark". Ratchets are far less expensive to hedge than are roll ups. The most value from*

a ratchet feature accrues before participants retire and begin taking withdrawals from their accounts.

8. *What are the advantages and disadvantages for participants of selecting Lifetime Income payments through a plan (in-plan option) as opposed to outside a plan (e.g., after a distribution or rollover)?*

In Plan Option:

Advantages:

- *Institutional pricing (lower than retail).*
- *Company has fiduciary and oversight responsibilities with respect to the provider.*
- *Less predatory marketing practices.*
- *Incremental/less drastic change (no roll over process) – a continuation of investing with a known entity and plan.*
- *Access to independent advice.*
- *In-Plan options can be structured to avert the behavioral biases of participants such as herding behavior and status quo bias.*
- *Opt-out defaults which include Lifetime Income will result in broader adoption specifically because of behavioral biases.*
- *No gender discrimination in pricing.*
- *Flexibility to buy-in to an option pre-retirement and get a better rate.*

Disadvantages:

- *Reduced number of choices. The participant must go with the product and the company(s) selected as the provider.*
- *Opt- in design which include Lifetime Income will result in lower adoption, in the absence of other incentives, specifically because of behavioral biases.*

Out of Plan Option:

Advantages:

- *Freedom to choose provider and options of the annuity.*
- *Ability to consolidate all assets.*

Disadvantages:

- *Offers only retail pricing.*
- *Individual is responsible for selection and oversight of the provider, including assessment of the financial strength of the provider.*
- *Individuals need to move their assets and make a decision.*
- *May be subject to predatory marketing practices and selling pressure.*
- *Do not have access to institutional independent advice.*
- *Lack of reliable benchmarks or reference points for comparison.*

9. What are the advantages and disadvantages from the standpoint of the plan sponsor of providing an in-plan option for lifetime income as opposed to leaving to participants the task of securing a lifetime income vehicle after receiving a plan distribution?

<u>In Plan Option:</u>

Advantages:

- *Greater assets (through retention of participants in plan) create pricing efficiencies.*
- *Professional staff negotiate product with vendor avoiding predatory practices.*
- *The DC plan begins to look like the Defined Benefit plan and becomes a substitute for a frozen DB plan.*
- *Provides employer another tool to maintain competitive benefits and manage the workforce.*
- *Many of the advantages that accrue directly to participants may indirectly help plan sponsors by increasing employee satisfaction and retention.*

Disadvantages:

- *Plan sponsor has fiduciary (provider credit default potential) and oversight responsibility for the product and vendor. It also adds to the plan sponsor's work load and cost.*
- *Lack of adoption among peer companies poses material headline risk, employee relations issues and exposure to legal action in the event of unforeseen negative results.*
- *Products continue to develop at a rapid pace and design improvements continue to emerge.*
- *There is a lack of understanding with regard to current safe harbor guidance. The fiduciary cannot control future events. Sponsors may face legal risk even if they have chosen annuity provider(s) prudently.*
- *Current safe harbor guidance must be improved to explicitly recognize more Lifetime Income designs.*
- *There is a lack of broad consensus among plan sponsors and product providers on standards.*

<u>Out of Plan Option:</u>

Advantages:

- *Plan sponsor relinquishes role as fiduciary and no longer has oversight responsibility for the product and vendor.*
- *Established offerings, record keeping, systems, reporting, etc. exist.*

Disadvantages:

- *Fewer assets allow for less pricing efficiencies.*

- *Individuals could be subject to unscrupulous marketing practices.*
- *No control of quality of products that participants end up choosing.*

10. How commonly do plan sponsors offer participants the explicit choice of using a portion of their account balances to purchase a lifetime annuity, while leaving the rest in the plan or taking it as a lump sum distribution or a series of ad hoc distributions? Why do some plan sponsors make this partial annuity option available while others do not? Would expanded offering of such partial annuity options -- or particular ways of presenting or framing such choices to participants -- be desirable and would this likely make a difference in whether participants select a lifetime annuity option?

- *Partial annuitization may be suitable for some plan participants. It allows participants to have some guaranteed income, while preserving the potential for remaining assets to provide a buffer against future inflation.*
- *However, participants will continue to be faced with many of the same obstacles to utilization, albeit to a somewhat lesser degree.*
- *Participants may prefer partial annuities because it leaves them with assets to deal with emergencies and/or to bequeath to their heirs.*
- *Some providers of irrevocable annuity products support the idea of partial annuitization over full annuitization due to the uncertainties that surround retirement income adequacy.*
  It is very important to note that participant-directed Defined Contribution plan participants enjoy a valuable design benefit in the freedom they have to make choices and subsequently change their minds at any point in the future. Some would argue that this design feature should extend into Lifetime Income options as well. There is most certainly a cost to maintaining this flexibility.

11. Various "behavioral" strategies for encouraging greater use of lifetime income have been implemented or suggested based on evidence or assumptions concerning common participant behavior patterns and motivations. These strategies have included the use of default or automatic arrangements (similar to automatic enrollment in 401(k) plans) and a focus on other ways in which choices are structured or presented to participants, including efforts to mitigate "all or nothing" choices by offering lifetime income on a partial, gradual, or trial basis and exploring different ways to explain its advantages and disadvantages. To what extent are these or other behavioral strategies being used or viewed as promising means of encouraging more lifetime income? Can or should the 401(k) rules, other plan qualification rules, or ERISA rules be modified, or their application clarified, to facilitate the use of behavioral strategies in this context?

- *Behavioral strategies (especially default provisions), when combined with education, will help increase assets in Lifetime Income options.*
- *Clarification of acceptable behavioral design standards will increase the confidence of plan sponsors who might be aware of their potential benefits, but would otherwise forego implementing them for fear of censure and/or legal exposure.*

12. How should participants determine what portion (if any) of their account balance to annuitize? Should that portion be based on basic or necessary expenses in retirement?

- *Individual flexibility should be maximized due to different levels of other resources (private savings, additional retirement accounts, including spouses' accounts).*
- *Lifetime distribution options should secure income for basic, necessary expenses. It should also provide the same level of liquidity to allow participants to draw down assets when an unexpected need arises.*

13. Should some form of lifetime income distribution option be required for defined contribution plans (in addition to money purchase pension plans)? If so, should that option be the default distribution option, and should it apply to the entire account balance? To what extent would such a requirement encourage or discourage plan sponsorship?

- *Each Defined Contribution plan and its population of participants are subject to unique circumstances. It would be imprudent to assume that all DC plans are appropriate vehicles for Lifetime Income to participants.*
- *There should be no additional requirements for plan sponsors. Any lifetime income option could discourage plan sponsorship, due to the complex nature of the options and potential risks associated with them.*

14. What are the impediments to plan sponsors' including lifetime income options in their plans, e.g., 401(k) or other qualification rules, other federal or state laws, cost, potential liability, concern about counterparty risk, complexity of products, lack of participant demand?

- *All of the above plus:*
    - *There is limited first mover advantage. It makes better sense for others to work out the operational and investment kinks.*
    - *While work is currently underway to assess various designs to offer Lifetime Income through Defined Contribution plans, many products continue to evolve and have not been around long enough and/or not used sufficiently to provide a good basis for assessment.*
    - *Concern about credit risk of the insurance provider. Are the assets protected in a bankruptcy and who will provide the income for life if the annuity provider no longer exists? Is the state insurance guaranty system sufficient to handle a large company and/or several smaller company failures in a short period of time?*
    - *With uncertainty about the ability of the state guaranty system to handle several failures, there is limited information about reinsurance in the plan context.*
- *Current safe harbor provisions are imprecise and difficult to apply to various products currently under consideration, specifically guaranteed lifetime/minimum withdrawals benefits (GLWB or GMWB). More clarity and revised guidelines that specifically apply to those products in all phases of their life cycle (not just in the insurer payout phase) will enable plan sponsors to select products without fear of undue liability.*

- *State insurance laws differ and some product designs may be approved in some states, but not others. Standard design features should be agreed to and available for plans with participants in all states.*
- *State insurance guaranty associations provide little clarity on how GLWB/GMWB products would be valued in the event of insurer insolvency prior to the point where an insurer is paying benefits to a participant. The Agencies would provide invaluable assistance to plan sponsors by working with various guaranty associations and the National Organization of Life and Health Insurance Guaranty Associations (NOLHGA) to develop and communicate a clear policy as it relates to valuing such instruments in all phases of their life cycle.*
- *To date, participants have shown little interest in Lifetime Income options.*

15. What are the advantages and disadvantages of approaches that combine annuities with other products (reverse mortgages, long term care insurance), and how prevalent are these combined products in the marketplace?

Disadvantages:

- *Each of these products can be complex, and bundling them ratchets up the overall complexity exponentially, both for the plan sponsor and the participant.*
- *High quality / low cost providers of each type of product may be different, offering little advantage to bundling.*
- *The vast array of participants' overall financial situations and needs makes it extremely difficult to determine which bundled solutions might be useful, and likely leads to very low usage of any particular bundled solution.*
- *Some products (such as reverse mortgages) may be ill-advised for many participants, and could appear to be endorsed by the sponsor*

16. Are there differences across demographic groups (for example men vs. women) that should be considered and reflected in any retirement security program? Can adjustments for any differences be made within existing statutory authority?

Participant Education

The Department of Labor issued Interpretive Bulletin 96-1 (29 CFR 2509.96-1) to clarify that the provision of investment education, as described in the Bulletin, will not be considered the provision of "investment advice," which would give rise to fiduciary status and potential liability under ERISA for plan participants' and beneficiaries' investment decisions.

17. What information (e.g., fees, risks, etc.) do plan participants need to make informed decisions regarding whether to select lifetime income or other arrangements designed to provide a stream of income after retirement?

- *Education about turning account balances into income streams.*
- *Education about the various products available to provide Lifetime Income (including fees guarantees and features).*

- *Information about insurer credit risk and any reinsurance coverage or state guarantees.*
- *Education about longevity risk and approaches to mitigating this risk.*
- *Education about participant sensitivity to the sequence of investment returns they experience and the particular risks posed by negative market returns in the years approaching and immediately after retirement.*
- *Modeling and or advice resources to compare products under various scenarios.* (*It should be noted that it is not in outside investment advisors interest to have participants move money into an annuity which lowers the base for their fees or eliminates the need for their services.)*

When and how (i.e., in what form) should it be provided?

- *Web sites, 800-number during business hours, occasional emails / mailings.*

What information currently is provided to participants, who typically provides it, and when and how is it provided to them?

- *Currently, most participants receive quarterly information or on-demand Web updates from the plan sponsor and/or the recordkeeper regarding fund investments which may include account market value, performance, fees, risks, commentary, top sectors/countries, etc. At a bare minimum, the Lifetime Income product information should be communicated at the same frequencies using the same parameters. Additionally, the lifetime income product should include an explanation of how it works, who may want to use it and why. Plan sponsors may also want to consider educational webinars or live meetings to explain the product and field questions.*

18. Is there a need for guidance, regulatory or otherwise, regarding the extent to which plan assets can be used to pay for providing information to help participants make informed decisions regarding whether to select Lifetime Income or other arrangements designed to provide a stream of income after retirement, either via an in-plan or out-of plan option?

- *Yes, it would be helpful if there was specific and clear guidance that allowed for education materials to be paid from plan assets rather than by the plan sponsor.*

19. What specific legal concerns do plan sponsors have about educating participants as to the advantages and disadvantages of lifetime income or other arrangements designed to provide a stream of income after retirement? What actions, regulatory or otherwise, could the Agencies take to address such concerns?

- *Liability concerns relative to when education becomes advice.*
- *Establish safe harbor rules to eliminate liability to sponsor.*

20. To what extent should plans be encouraged to provide or promote education about the advantages and disadvantages of lifetime annuities or similar lifetime income products, and what guidance would be helpful to accomplish this?

Disclosing the Income Stream that Can be Provided from an Account Balance

ERISA section 105 requires defined contribution plans to furnish to each participant an individual benefit statement, at least annually, that includes the participant's "accrued benefits," i.e., the individual's account balance.

21. Should an individual benefit statement present the participant's accrued benefits as a lifetime income stream of payments in addition to presenting the benefits as an account balance?

- *Such a display would be helpful to participants.*
- *Sponsors should be provided safe harbors on making income projections due to the number of assumptions that need to be made.*

22. If the answer to question 21 is yes, how should a lifetime stream of income payments be expressed on the benefit statement? For example, should payments be expressed as if they are to begin immediately or at specified retirement ages?

- *Both immediate and projected would be helpful. However, it should be made clear that future contributions by either the plan sponsor and/or the participant are not guaranteed.*

Should benefit amounts be projected to a future retirement age based on the assumption of continued contributions?

- *Yes; Underlying assumptions should be clearly specified.*

Should lifetime income payments be expressed in the form of monthly or annual payments? Should lifetime income payments of a married participant be expressed as a single-life annuity payable to the participant or a joint and survivor-type annuity, or both?

- *Monthly and annual payments would support the educational effort around Lifetime Income options.*
- *Both single life and Joint &Survivor forms could be shown as well as the impact of taking early and deferred retirements on benefit payments.*

23. If the answer to question 21 is yes, what actuarial or other assumptions (e.g., mortality, interest, etc.) would be needed in order to state accrued benefits as a lifetime stream of payments?

If benefit payments are to commence at some date in the future, what interest rates (e.g., deferred insurance annuity rates) and other assumptions should be applied? Should an expense load be reflected?

- *The interest rate assumption should be the same as used by the underlying Lifetime Income option to project benefit payments and hedge market exposures.*

Are there any authoritative tools or sources (online or otherwise) that plans should or could use for conversion purposes, or would the plan need to hire an actuary?

Should caveats be required so that participants understand that lifetime income payments are merely estimates for illustrative purposes?

- *Yes.*

Should the assumptions underlying the presentation of accrued benefits as a lifetime income stream of payments be disclosed to participants?

- *Yes.*

Should the assumptions used to convert accounts into a lifetime stream of income payments be dictated by regulation, or should the Department issue assumptions that plan sponsors could rely upon as safe harbors?

- *Regulations would be too inflexible to account for all situations.*
- *A reasonable safe harbor would use the same assumptions as the underlying Lifetime Income option is using to project benefit payments and hedge market exposures.*

24. Should an individual benefit statement include an income replacement ratio (e.g., the percentage of working income an individual would need to maintain his or her pre-retirement standard of living)? If so, what methodology should be used to establish such a ratio, such as pre-retirement and post-retirement inflation assumptions, and what are the impediments for plans to present the ratio in a meaningful way to participants on an individualized basis?

- *Since replacement ratios at the plan level do not take into account other assets (Social Security, private savings, and other sources of retirement income) or individual liabilities (heath care/long-term care costs) they can be misleading. Plans sponsors may have difficulty communicating effectively about replacement ratios and how they should be used.*
- *It should be at the option of the plan sponsor on whether to not to include a replacement ratio.*

<u>401(k) and Other Plan Qualification Rules</u>

Income Tax Regulations that apply specifically to lifetime annuities include: 26 CFR 1.401(a)-11, 26 CFR 1.401(a)-20, 26 CFR 1.401(a)(9)-1 through 26 CFR 1.401(a)(9)-9, 26 CFR 1.417(a)(3)-1, and 26 CFR 1.417(e)-1.

25. How do the 401(k) or other plan qualification rules affect defined contribution plan sponsors' and participants' interest in the offering and use of lifetime income? Are there changes to those rules that could or should be made to encourage lifetime income without prejudice to other important policy objectives?

- *Establish clear safe harbor rules to eliminate liability to sponsor.*

26. Could or should any changes be made to the rules relating to qualified joint and survivor annuities and spousal consents to encourage the use of lifetime income without compromising spousal protections?

- *Retain spousal consent rules in Defined Benefit plans.*

27. Should further guidance clarify the application of the qualified joint and survivor annuity rules or other plan qualification rules to arrangements in which deferred in-plan insurance annuities accumulate over time with increasing plan contributions and earnings?

28. How do the required minimum distribution rules affect defined contribution plan sponsors' and participants' interest in the offering and use of lifetime income? Are there changes to those rules that could or should be made to encourage lifetime income without prejudice to other important policy objectives? In particular, how are deferred annuities that begin at an advanced age (sometimes referred to as longevity insurance) affected by these rules? Are there changes to the rules that could or should be considered to encourage such arrangements?

29. Are employers that sponsor both defined benefit and defined contribution plans allowing participants to use their defined contribution plan lump sum payouts to "purchase" lifetime income from the defined benefit plan? Could or should any actions be taken to facilitate such arrangements? Should plans be encouraged to permit retirees who previously took lump sums to be given the option of rolling it back to their former employer's plan in order to receive annuity or other lifetime benefits?

- *Generally, employers do not allow participants to use DC assets to "purchase" Lifetime Income from the Defined Benefit plan. In fact, many plan sponsors would like to transfer much of the risk associated with the DB plan and not add to the liabilities. Some plans are underfunded and should not be required to add to that burden by increasing DB liability exposure.*
- *This provision would not be attractive to plan sponsors since roll-over contributions or returning lump sum benefits would increase plan liabilities and thus increase the plan sponsor risks related to their net income volatility, funding ratio volatility and contribution requirements. In addition to raising the overall amount of liabilities, allowing participants to roll money into the DB plan introduces another variable into the projection of future liabilities and even more uncertainty, especially since participants would be more likely to use this option during or following times of market weakness and/or volatility.*
- *For the reasons stated above, DB plans should not be encouraged to permit retirees who previously took lump sums to be given the option of rolling it back to their former employer's plan in order to receive an annuity or other lifetime benefits.*
- *Further, there is some question about how Pension Benefit Guaranty Corporation (PBGC) guarantees apply to employee roll-overs. While employee contributions are paid first by PBGC, there is a question about whether any annuity benefits 'bought' by the participant would affect guaranteed benefits.*
- *Lastly, there would be a large cost involved to update recordkeeping systems and company systems in order to implement such proposed changes.*

Selection of Annuity Providers

The Department of Labor's regulation 29 CFR 2550.404a-4 contains a fiduciary safe harbor for the selection of annuity providers for the purpose of benefit distributions from defined contribution plans.

30. To what extent do fiduciaries currently use the safe harbor under 29 CFR 2550.404a-4 when selecting annuity providers for the purpose of making benefit distributions?

31. To what extent could or should the Department of Labor make changes to the safe harbor under 29 CFR 2550.404a-4 to increase its usage without compromising important participant protections? What are those changes and why should they be made?

- *The current safe harbor should be improved to recognize more Lifetime Income designs.*
- *Further, the safe harbor must explicitly protect fiduciaries from liability resulting from negative future events that could not be foreseen.*

32. To what extent could or should the safe harbor under 29 CFR 2550.404a-4 be extended beyond distribution annuities to cover other lifetime annuities or similar lifetime income products? To which products should or could the safe harbor be extended?

ERISA Section 404(c)

ERISA section 404(c) and 29 CFR 2550.404c-1 provide defined contribution plan fiduciaries with limited relief from the fiduciary responsibility provisions of ERISA where a participant or beneficiary exercises control over the assets in his or her account.

33. To what extent are fixed deferred lifetime annuities (i.e., incremental or accumulating annuity arrangements) or similar lifetime income products currently used as investment alternatives under ERISA 404(c) plans? Are they typically used as core investment alternatives (alternatives intended to satisfy the broad range of investments requirement in 29 CFR 2550.404c-1) or non-core investment alternatives? What are the advantages and disadvantages of such products to participants? What information typically is disclosed to the participant, in what form, and when? To what extent could or should the ERISA 404(c) regulation be amended to encourage use of these products?

34. To what extent do ERISA 404(c) plans currently provide lifetime income through variable annuity contracts or similar lifetime income products? What are the advantages and disadvantages of such products to participants? What information about the annuity feature typically is disclosed to the participant, in what form, and when? To what extent could or should the ERISA 404(c) regulation be amended to encourage use of these products?

Qualified Default Investment Alternatives

ERISA section 404(c)(5) provides that, for purposes of ERISA section 404(c)(1), a participant in a defined contribution plan will be treated as exercising control over the assets in his or her account with respect to the amount of contributions and earnings if, in the absence of an investment election by the participant, such assets are invested by the plan in accordance with regulations of the Department of Labor. The Department of Labor's regulation 29 CFR 2550.404c-5 describes the types of investment products that are qualified default investment alternatives under ERISA section 404(c)(5).

35. To what extent are plans using default investment alternatives that include guarantees or similar lifetime income features ancillary to the investment fund, product or model portfolio, such as a target maturity fund product that contains a guarantee of minimum lifetime income? What are the most common features currently in use? Are there actions, regulatory or otherwise, the Agencies could or should take to encourage use of these lifetime income features in connection with qualified default investment alternatives?

- *Investments with Lifetime Income features should be explicitly allowed as a QDIA.*

Comments Regarding Economic Analysis, Regulatory Flexibility Act, and Paperwork Reduction Act

Executive Order 12866 (EO 12866) requires an assessment of the anticipated costs and benefits of a significant rulemaking action and the alternatives considered, using the guidance provided by the Office of Management and Budget. In addition, the Regulatory Flexibility Act (RFA) may require the preparation of an analysis of the economic impact on small entities of proposed rules and regulatory alternatives. For this purpose, the Agencies consider a small entity to be an employee benefit plan with fewer than 100 participants. The Paperwork Reduction Act (PRA) requires an estimate of how many "respondents" will be required to comply with any "collection of information" requirements contained in regulations and how much time and cost will be incurred as a result. The Agencies in this section of the RFI are requesting comments that may contribute to any analyses that may eventually need to be performed under EO 12866, RFA, and PRA, both generally and with respect to specific areas identified in questions 36 through 39.

36. What are the costs and benefits to a plan sponsor of offering lifetime annuities or similar lifetime income products as an in-plan option? Please quantify if possible.

37. Are there unique costs to small plans that impede their ability to offer lifetime annuities or similar lifetime income products as an in-plan option to their participants? What special consideration, if any, is needed for these small entities?

38. Would making a lifetime annuity or other lifetime income product the default form of benefit payment have an impact on employee contribution rates? If so, in which direction and why?

- *The designation of a Lifetime Income option as a default form of benefit payment from a Defined Contribution plan could have a measurable impact on individual employee contribution rates. However, it is entirely possible that the magnitude of this impact would be difficult to discern at the plan level.*
- *Some may increase their contribution rates if they believed their current contribution levels (and/or investment returns) are insufficient to fund an acceptable standard of living in retirement. Others, however, might conclude that the Lifetime Income product provides enough to establish an acceptable standard of living in retirement thereby freeing them to redirect some of their savings to other consumption.*

39. For plans that offer lifetime annuities or similar lifetime income products, what percentage of eligible workers elect to annuitize at least some of their retirement assets and what percentage elect to annuitize all of their assets?