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April 30, 2010

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

Attn: Lifetime Income RFI
Subject: RIN 1210-AB33

E-mail to e-ORI@dol.gov

Ladies and Gentlemen:

Horizon Investments, LLC ("Horizon") appreciates the opportunity to respond to your Request for Information regarding Lifetime Income Options for Participants and Beneficiaries in Retirement Plans.

Horizon Background

William Breen, emeritus Professor of Finance at Northwestern University's Kellogg Graduate School of Management and Senior Investment Strategist at Horizon Investments, has done extensive research and testing of lifetime income strategies for over 20 years. The original research was done in connection with Breen's portfolio management class at Kellogg. The models he developed demonstrated non-mean variance solutions to portfolio problems with asymmetric costs. Professor Breen has been presenting these models in MBA classes and in executive education classes at Kellogg since the middle 1980's. Now retired from Kellogg, he also uses this research for his own retirement planning.

Summary of Comments

Why is lifetime income underutilized?

There are four answers to this question:

- Participants who have insufficient retirement funds. The capital cost of an annuity with a guaranteed lifetime income option for a 65 year old earning $75,000 per year is estimated at $1,586,468[1]. This is far in excess of typical retirement plan accounts, making the option affordable to only a small portion of the workforce. If extended to the entire workforce, the capital cost is estimated at $159 trillion for a twenty-year retirement life. Alternatively, if the

[1] Result based on DALBAR model using the following assumptions: Replacement income at retirement of $75,000, 3 percent inflation, 6 percent rate of return, 3 percent M&E, retirement age of 65 and life expectancy of 85 years.

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income is funded only when the cash is needed (such as in a government guarantee) the cost is estimated to be $273 trillion.

- Participants who have sufficient retirement funds. Retirees who have adequate capital to purchase an annuity with a guaranteed lifetime income option may prefer a pre-packaged Personal Retirement Income Strategies that are described in the next section. This alternative seeks flexibility, liquidity and portability, as well as a solution to the risk of inflation.

- Plan sponsors who have prohibition. Plan sponsors and other fiduciaries may fail their fiduciary duty[2] to diversify if a single or a limited number of companies were used to guarantee a lifetime income option. The exposure to liability is a strong disincentive for employers to include only one type of lifetime income option in their retirement plans. Employers have no economic incentive to take on the cost, burden and risk involved.

- Plan sponsors who feel no responsibility. Plan sponsors, as a general rule, do not consider employees' post retirement income to be their responsibility. Plan sponsors are highly reluctant to adopt any programs that would imply such a responsibility.

What needs to be done to increase utilization?

Increasing utilization involves making lifetime income products less burdensome for participants and plan sponsors and positioning them as an income supplement and not a total solution. This re-positioning will avoid setting unrealistic expectations of fully funding a luxurious retirement but instead define lifetime income as a valuable supplemental benefit.

For lifetime income to be less burdensome for participants of DB, DC and IRAs, the option must:

- Permit plan fiduciaries (Under ERISA 3(38) or 3(21) to advise retiring participants without restrictions.[3]

- Be simple enough as to not require additional education.

[2] Under Section 404(a)(1)(B) of the Employee Retirement Income Security Act of 1974 (ERISA), a fiduciary in charge of investment of a retirement plan's assets generally must make sure that the plan's assets are diversified so as to minimize the risk of large losses. A fiduciary of a retirement plan is defined in ERISA Section 3(21) to include any person who exercises any discretionary authority or control respecting management or disposition of the plan or its assets.

[3] Advisory Opinion 2005-23A restricts existing plan fiduciaries from advising participants under certain circumstances. An adviser (who is a fiduciary) that recommends that a plan participant rollover his or her account balance to an IRA or who "responds to participant questions concerning the advisability of taking a distribution or the investment of amounts withdrawn from the plan" could violate ERISA's prohibited transaction rules, if the adviser will earn fees on the IRA assets after a plan participant rolls over his or her account balance to the IRA.

- Adapt to the participants specific needs without the need for the participant to perform his/her own complex analysis.
- Occur automatically so that the un-engaged participant is enrolled into a default plan that is calculated to meet his/her estimated needs.
- Provide a simple exit for those participants who are automatically defaulted.

Making lifetime income less burdensome for employer sponsored plans requires:

- Providing fiduciary protection in the selection and monitoring of these options.
- Transferring employee out of the plan at retirement.
- Providing a positive incentive for employers to adopt this option.

Matters Germane to the Agencies' Consideration of Lifetime Annuities

As requested in the RFI, we have included the following matters for your consideration. For each subject, we have indicated why we believe it to be germane.

Personal Retirement Income Strategies

While it is clear that a lump sum distribution to an employee at retirement is an ineffective approach and fraught with risks, there is more than one way to address this problem. The approach contemplated in the RFI is the use of an annuity offering guaranteed lifetime income. A non-insured alternative, however, is available in the form of a disciplined investment approach, Personal Retirement Income Strategies ("PRIS") and may be more suitable for certain retirees. In fact, many retirees who elect a lump sum distribution actually wisely use the capital in a Personal Retirement Income Strategy.

PRIS refers to a variety of investment strategies that are pre-packaged for retirees. This packaging relieves the retirees' burden of investment decisions and adds the discipline necessary to prevent excessive draw-down of retirement capital. Within these packages assets are professionally managed to provide lifetime income as well as achieve other personal goals. The retiree does, however, retain ultimate control and can switch from one PRIS to another or change the parameters if/when circumstances change.

While certain PRIS strategies incorporate the same investment methods used by insurance companies to manage the capital for lifetime income options, they also utilize a number of other innovations and are sufficiently flexible to incorporate new techniques that are yet to be contemplated.

The underlying premise of a PRIS is that retirees should have the flexibility to tailor their investments to meet their personal situation; self-insuring without the necessity of engaging the insurance industry in the traditional fashion. PRIS has the following relevant benefits:

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- Meeting fiduciary obligations: Plan sponsors and other fiduciaries can meet their obligation to diversify plan investments since the participant is not permanently reliant on the success of a single company offering the lifetime income guarantee. Indeed, a key benefit of a PRIS is that it could be structured so as to utilize a plan's existing investment options.

- Superior inflation adjusted spending outcomes: A PRIS can be changed to meet changes in spending needs that differ from forecasts.

- Liquidity: A PRIS provides access to capital throughout the retiree's lifetime to handle changes in personal situation and priorities.

- Portability: A PRIS permits the retiree to change from one investment provider to another at any time the retiree chooses.

- No issuer risk: A PRIS avoids the risk of a single insurer's failure through a diversified investment portfolio.

- Fee efficiency: The underwriting and behavioral risks that are part of the cost of a guarantee are eliminated because of the self-insured nature of a PRIS.

For these reasons, we believe that PRIS should be recognized and treated as a lifetime income alternative along side insurance solutions.

Decision Support

The major decision that workers must make at retirement is whether to purchase a guarantee for lifetime income and/or to use a PRIS. In making this critical decision, the worker should consider the costs, risks and benefits of both options. The answers to the following questions will help workers to make an informed decision:

- Is there sufficient capital available to pay for a guarantee and maintain the desired standard of living?

- What are the alternatives available if un-guaranteed funds are depleted?

- Are changes likely to occur in the future that will require either more or less income than is currently anticipated?

- Is it important to provide inheritance for others?

- Will there ever be a need to change providers or investment strategies?

- Is there likely to be a need for extra cash?

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Inflation Threat

In addition to the loss of buying power, inflation poses another threat to retirees that rely on annuities for lifetime income. The analysis by Horizon shows that some insurance solutions are particularly vulnerable to inflation.

Horizon has examined the spending outcomes of the Horizon Income Strategy compared to a standard variable annuity contract over all historical 20 year periods beginning in the third quarter of 1926, and ending first quarter of 2010. The spending outcomes of the Horizon Income Strategy were scaled so that the starting and (real) ending wealth for both strategies were approximately the same over each 20 year period. Whenever inflation over a period exceeded the long run average inflation, the variable annuity average spending was significantly less in real terms than the Horizon Income strategy spending.

RFI Questions & Answers

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:

- *Provide income supplement for life*
- *Eliminate/reduce the need to manage retirement funds*

Disadvantages

- *Few participants have sufficient capital at retirement to replace a paycheck for life, including increases in cost of living.*
- *Little flexibility to change after making commitment*
- *Inheritance for heirs is compromised*
- *Participant's inability to use diversification to protect themselves from large losses*

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? 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.)? 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?

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Cause of low usage by participants

- *Insufficient capital to fund lifetime income. Replacement income of $75,000 today would require an annuity that cost $1.59 million (See footnote 1). This capital far exceeds lump sum available to most retiring participants.*
- *Preference for Personal Retirement Income Strategy. Many retirees who elect a lump sum distribution do so because of professional advice. Professionals explain the advantages of maintaining flexibility and portability as well as a higher income level and the ability to pass the unspent capital on to heirs.*
- *Employers have disincentive to offer lifetime income. Employers who offer lifetime income options must bear the cost, liability and loss of flexibility for employees that are no longer part of the work force.*
- *Restrictions on advisers to advise on rollovers. The conflict of interest prohibition (see footnote 3) place on investment fiduciaries to advise on rollovers causes these experts to avoid the retirement transition and thus leave the participants with no guidance.*

Effect of other factors on low usage

- *Cost: Even if participants receive the best possible value (zero profit margin for insurer), there is insufficient capital ($1.26 million[4] at $75,000 per year) to adequately fund lifetime income.*
- *Complexity of products: Complexity is not a deterrent to usage since usage is primarily driven by professional recommendations or availability from the employer and not "self-serve" shopping.*
- *Adverse selection, poor decision-making by consumers: Participant decisions are almost always based on professional recommendations, so that poor decisions apply in cases where there are inappropriate recommendations.*
- *Desire for flexibility to respond to unexpected financial needs: Flexibility is a frequent objection to professional recommendations since a large proportion of capital becomes inaccessible.*
- *Counterparty risk of seller insolvency: Insolvency is a concern, particularly following the financial crisis of 2008.*

[4] Result based on DALBAR model using the following assumptions: Replacement income at retirement of $75,000, 3% inflation, 6% rate of return, 0% M&E, retirement age of 65, life expectancy of 85.

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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?

Lifetime income options available

- *Guaranteed Income: The payments are underwritten by an insurance company and often re-insured by a pool of insurers. The entire risk of outliving the capital is borne by the insurer since alternatives available to participants[5] do not change the underwriting risk.*
- *Personal Retirement Income Strategy ("PRIS"): Withdrawals are distributed over a certain period (life expectancy) and participant has the benefit of additional appreciation and passing unused portion to heirs. The capital required for a PRIS is lower than the guaranteed option since the participant can consider alternatives that an insurer cannot. (See footnote 5)*

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?

Lifetime income options provided at retirement

- *Lifetime income options are generally not provided within an employer sponsored defined contribution plan.*
- *Such options are generally offered to retirees individually upon exiting the plan.*

Lifetime income options provided during accumulation phase

- *Employer sponsored defined contribution plans generally do not offer lifetime income options either during accumulation or at retirement.*

Structure of accumulating annuity arrangements

- *Such structures are rare.*

[5] Alternatives available to participants consist of changes that a participant can make in the event that income is reduced. These include returning to the work force, liquidate other assets (such as real estate through reverse mortgages), reduce spending, draw from estate or rely on family or government. These alternatives are not considered if the participant's risk of outliving income is protected by a guarantee.

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

Extent to which employer sponsored defined contribution plan participants can choose a lifetime income option

- *Lifetime income options are generally not provided within an employer sponsored defined contribution plan.*

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?

Types of lifetime income options available after receiving lump sum distributions

- *Guaranteed Income Options. These take the form of annuities where some or all of a predetermined payout is guaranteed. This approach includes an extra cost for insurance.*
- *Personal Retirement Income Strategies ("PRIS"). Participants are provided with an investment/withdrawal strategy that supports a higher standard of living but could require using behavioral alternatives. See footnote 5.*

Structure of lifetime income options available after receiving lump sum distributions

- *Guaranteed Income Options are offered as fixed, inflation adjusted, variable, immediate or deferred.*
- *Personal Retirement Income Strategies ("PRIS") contain an investment portfolio and a withdrawal plan that can be predetermined or made to vary based on changing needs, priorities and market conditions.*

Can annuity purchase rights available under an employer sponsored defined contribution plan be retained after receiving lump sum distributions?

- *The economies of scale applicable to a retirement plan can rarely be applied to the individual servicing needs, post retirement.*

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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?

Cost impact of features

- *A cost consideration of insured lifetime income products is the guarantee. This cost has two components, the underwriting risk and the behavioral cost. The underwriting risk is estimated to be 21 percent of the participant's capital. The behavioral cost represents the alternatives available to participants if capital is inadequate. (See footnote 5)*
- *Lifetime payments represent 79 percent of the capital cost of a guaranteed option*
- *The remaining 21 percent represents the cost of the guarantee and servicing cost. The guarantee cost includes extended life and acceleration options.*

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)?

Advantages of in-plan lifetime income option for participants

- *Ease of selection (especially if set as default)*
- *Recourse to employer in the absence of proper procedural prudence, should insurer fail.*

Disadvantages of in-plan lifetime income option for participants

- *Higher plan costs to current work force that bear the cost for retired workers.*
- *Lower availability since it is less likely to be adopted by the plan sponsor*

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?

Advantages to plan sponsor of in-plan lifetime income option

- *None*

Disadvantages to plan sponsor of in-plan lifetime income option

- *Potential prohibited transaction violation for failure to carry out the fiduciary duty to diversify investments since this option often relies on the success of one company.*
- *Higher cost since costs and responsibility continue past retirement*

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- *Liability for selecting a guaranteed lifetime income option is indefinite*
- *Loss of flexibility to change providers in the future*

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?

How common is option to choose a lifetime annuity with only a portion of the account balance

- *Lifetime income options are generally not provided within an employer sponsored defined contribution plan.*

Why some plan sponsors make this option available

- *Very few do*

The difference such an option would make to the usage of a lifetime annuity

- *Such an option would materially increase usage if pre-calculated for the participant up to the amount required to replace the salary at retirement.*

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?

Current usage of behavioral strategies

- *Default or automatic arrangements: Low/no usage*
- *Mitigate "all or nothing" choices: Low/no usage*
- *Lifetime income on a partial basis: Low/no usage*
- *Lifetime income on a gradual basis: Low/no usage*
- *Lifetime income on a trial basis: Low/no usage*

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Promising behavioral strategies

- *Default or automatic arrangements: All empirical evidence indicates that a calculated default that is predicated on the participant's circumstance will produce the greatest increase in usage. This usage is limited by the capital available… participants with insufficient capital are not fully served.*
- *Mitigate "all or nothing" choices: Requires the failed practice of requiring the participant to be engaged,[6] educated and then make prudent choices. This is not expected to materially affect usage.*
- *Lifetime income on a partial basis: For the calculated default to be effective, it should automatically select the portion of an account that is utilized for lifetime income.*
- *Lifetime income on a gradual basis: While gradual implementation is effective during accumulation, arbitrary increase or decrease of lifetime income is counter productive. Changes should be made in response to the cost of living (inflation).*
- *Lifetime income on a trial basis: A trial basis is only effective if the trial is automatically extended into a permanent arrangement. This will provide a marginal increase in usage, but only from those participants who are engaged (See footnote 6).*

Modification/clarification of 401(k) rules

- *Provide class exemption from diversification requirement for purposes of lifetime income options. This exemption must define the specific structure, such as a diversified reinsurance guarantee in order to qualify for the lifetime income exemption.*
- *Revise Advisory Opinion 2005-23A (see footnote 3) to explicitly permit fiduciaries to advise participants entering retirement, recognizing that such a change is in the interest of the participants, even though it will require additional services from the adviser and associated additional compensation.*
- *Require qualified default investment alternatives ("QDIA") to include a calculated income estimate at-retirement that defaults to a lifetime income option outside of the plan in order for the QDIA to qualify for fiduciary liability protection.*

Modification/clarification of other rules

- *None*

[6] The term "engaged" refers to those employees who take an active interest in their finances and read and understand materials provided. The number of engaged employees depends largely on the composition of the work force and the expenditure made by the employers to achieve engagement. The percentage of engage employees typically varies from 5 percent to 35 percent.

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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?

How participants should determine how much to annuitize

- *Participants should have three choices, first is to do nothing and let a calculated default apply, second is to rely on a professional and third is to "self-serve."*
- *Most participants will elect the calculated default.*
- *Participants with complex situations will choose the professional, including investment fiduciaries of the plan.*
- *Knowledgeable and independent participants will "sel- serve".*

Should amount be based on basic or necessary retirement expenses?

- *"Necessary expenses" is highly subjective and varies with the participants own personal choices and should not be used as a basis.*
- *A calculated default should be based on replacing a percentage of current income. Current models typically use 85 percent.*

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?

Required distribution option

- *Some form of low cost lifetime income option should be required for retirement plans. Without such a requirement, plan sponsors are unlikely to undertake the expense and potential liability. For maximum uptake and minimum resistance, plan sponsors should be able to satisfy such a requirement with a low cost solution such as PRIS that avoids the cost of guarantees.*
- *A major weakness of QDIAs is the failure to require a distribution option. This should be corrected by requiring a low cost lifetime income default in order to qualify for QDIA treatment.*
- *Plans that choose to use a QDIA must also include a lifetime income alternative, whether guaranteed or PRIS.*

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Default distribution option

- *The default lifetime income option should be the low cost alternative so as not to burden the defaulted retiree or the plan with unnecessarily high costs. The cost can be kept lower if the default does not require a guarantee.*

Apply default to entire account

- *All assets (to the extent provided by the participant) should be considered in calculating the default and used only to the extent required to replace pre-retirement income as determined by the calculated default.*

Effect on discouraging/encouraging plan sponsorship

- *Plan sponsorship will be discouraged by fiduciary liability (see footnote 2) for the distribution options and additional costs, including liability insurance.*
- *Plan sponsorship can be encouraged by additional incentives that mean lower cost or lowered regulatory burdens.*

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?

Impediments to plan sponsors including lifetime income

- *<u>No benefit or incentive</u>: There is virtually no economic reason for plan sponsors to devote attention to an option that applies only to employees for whom the employer has no further responsibility and from whom nothing is expected in return. Plan sponsors are more likely to embrace a plan that ends the responsibility at retirement.*
- *<u>401(k) or other qualification rules</u>: Plan sponsors face potential prohibited transaction violations for failure to diversify investments (See footnote 2). Advisory Opinion 2005-23A also restricts the role of investment fiduciaries (see footnote 3) in advising retiring participants.*
- *<u>Other federal or state laws</u>: Laws and regulations that govern issuance of insurance contracts differ from one state to another and are an impediment.*
- *<u>Cost</u>: There is no economic justification to pay for services for past employees. The cost of retaining records of employees who are no longer productive for the employer will continue to be avoided.*
- *<u>Potential liability</u>: The un-measurable liability of participating in offering lifetime income is a daunting impediment. Plan sponsors are more likely to adopt a lifetime income plan in which retirees' assets are outside of the plan.*

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- *Concern about counterparty risk: Counterparty risk is one of plan sponsors' concerns of potential liability. This is eliminated if the plan sponsor offers a Personal Retirement Income Strategy that does not rely exclusively on guarantees.*
- *Complexity of products: Not material, when compared to other impediments.*
- *Lack of participant demand: Participant demand from currently active employees can provide an incentive, but there has been very little interest historically. Demand occurs at the point of retirement which is too late to be a material influence on the plan sponsor.*

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?

Advantages of combined products

- *There is added convenience for the "self serve" consumer of such products in being able to do business with one institution.*

Disadvantages of combined products

- *Few if any institutions can offer high quality products and expertise in all areas so use of combined products invariably involves a compromise of quality, expertise and cost.*

Prevalence

- *Such combinations are best made by professionals and not pre-packaged in the form of a product.*

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?

Demographic differences

- *While demographic differences are undeniable these are minor compared to situational differences that should be included in any calculated default. Such differences include lifestyle desires, marital status, minimum acceptable standards of living and post retirement activities.*

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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? When and how (i.e., in what form) should it be provided? What information currently is provided to participants, who typically provide it, and when and how is it provided to them?

Participant decision information

- *Most participants will face one major decision with respect to lifetime income, whether to use a Guaranteed Option or a PRIS. This decision is informed by the cost of the guarantee against the benefits of PRIS. This distinction is easily understood and should be presented in clear and simple terms.*
- *The experiment of providing participants extensive information with the expectation that they will make informed financial decisions has proven to be a colossal failure. The cost of efforts to date far exceeds any benefits derived.*
- *At the core of the problem is the lack of interest and engagement (See footnote 6) of the participant in either learning or in making financial decisions.*
- *Further pursuit of this folly is likely to produce the same unfortunate results.*

Form of information provided

- *Participants principally value and use two forms of assistance. The first is one that involves no decision-making (do it for me) and the second is a professional that recommends the course that best suits the individual. Very few analyze information provided and make informed decisions on their own.*

Information currently provided

- *Information currently provided consists of sales materials and that which is needed to meet regulatory requirements.*

When and how information is provided?

- *Information delivery is made to comply with regulatory requirements.*

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

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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?

Guidance in use of plan assets

- *Such guidance will serve only to further poor use of plan assets.*
- *Plan assets should be used to pay for services that participants value and actually use.*

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?

Concerns about educating participants

- *The major concern of plan sponsors is the ineffectiveness of this education. Recognizing the inadequacy, plan sponsors demand more and more education.*
- *The second concern is the loss of productivity associated with such education efforts.*

Agency actions

- *Agencies should require the use of calculated defaults and professional advice so that the need for participant education is minimized, costs reduced and better financial decisions made.*
- *Revise Advisory Opinion 2005-23A (see footnote 3) to explicitly permit fiduciaries to advise participants entering retirement, recognizing that such a change is in the interest of the participants, even though it will require additional services from the adviser and associated additional compensation.*

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?

Provide or promote education

- *The colossal failure of retirement education programs suggest that they should be discouraged and replaced with calculated defaults and professional advice.*

Guidance in promoting and providing education

- *Agencies should study the cost effectiveness of education programs and use the results to discourage reliance on them in their current form.*

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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?

Showing lifetime income stream on statements

- *Such a display would be highly beneficial if it were a calculated default. Participants should be shown two income streams, one based on guarantees and the other based on a Personal Retirement Income Strategy in order to illustrate the differences.*
- *Lifetime income stream should only be shown within 10 years of anticipated retirement.*

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

Format of lifetime income stream on statement

- *Income stream should be expressed as a percentage of projected income at the time of retirement and should reflect a forecast of future accumulation, returns and inflation.*
- *Using a percentage of projected income removes the need to decide if stream should be in the form of monthly or annual payments.*
- *Married participants should also receive a single percentage of projected needs.*

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

Underlying assumptions

- *The principal assumption for which participants have control is whether to use a Guaranteed Option or to use a Personal Retirement Income Strategy. Results based on each of these assumptions should be presented.*
- *Describing details of other underlying assumptions to participants is an abject waste. Underlying assumptions should be reviewed by fiduciaries that are then held accountable for them being reasonable.*
- *Participants interested in the assumptions should have access to them on request.*

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?

Income replacement ratio on statement

- *Income replacement ratio should be included starting at 10 years before anticipated retirement date. Earlier display of this is meaningless to the participant and is likely to be very inaccurate.*

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).

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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?

Actions Agencies should take to encourage inclusion of lifetime income options in QDIAs.

- *Provide a class exemption that relieves plan sponsors and other fiduciaries from liability with respect to diversification rules (see footnote 2).*

- *The current default alternatives address the accumulation of retirement assets but fail to include consideration for the critical pre-retirement employment stage. Employees that make no election are supported by the proposed regulation during working years but face an abrupt end to this support at the important decision of using those assets for retirement income.*

- *The current regulation is seriously flawed since the current default alternatives are inappropriate for an employee at retirement. The most important need at retirement is for lifetime income and this is true whether the employee is retiring at 40 or at 80 years old.*

- *Employees relying on the default will find that their retirement portfolio is very poorly structured to replace a paycheck for the rest of their lives.*
- *The Pension Protection Act requires that the default arrangement address the contributions and earnings in the plan but the current regulation fails to address the needs of employees at retirement, the time when a default is most urgently needed.*

- *The three current long term default alternatives should be amended to require an automatic transfer into an appropriate post-retirement fund or portfolio at the time employees retire.*

- *We suggest the following amendment to correct this problem:*

  Sec. 2550.404c-5(e) sets forth five requirements for qualified default investments, which should be amended by adding a sixth:

  (6) A qualified default investment alternative must include at least one investment product, portfolio or service that is designed to produce lifetime income for the purpose of replacing employment income at retirement. Employees who have made no election must be automatically transferred into a lifetime income investment product, portfolio or service upon retirement.

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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.

Plan sponsor costs for offering a lifetime income option include:

- *Administrative cost of altering the plan*
- *Increased operating cost during employment and after employees retire, unless this is paid by plan participants*
- *Exposure to litigation and liability if guarantees are included*

There are no visible benefits to the plan sponsor to offer lifetime annuities or similar lifetime income products.

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?

Small plans can be disproportionately burdened by guarantees since it is uneconomical for guarantee providers to examine each small plan. Instead, guarantee providers are likely to underwrite small plan guarantees on an overall worst case basis, making them as expensive as individual guarantees.

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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?

> *A lifetime income option default will increase contribution rates only if the participant is fully informed and has the flexibility to redeploy investments in the future as needs and circumstances change.*
>
> *A lifetime income option that restricts future changes in investments is more likely to decrease contribution rates.*

Thanking you in advance for considering these issues,

Very truly yours,

Name	Signature	Date
James Breen President, Horizon Fiduciary Services	James T Breen	4/30/2010