# The Institutional Retirement Income Council

**Submission To**

**The Employee Benefits Security Administration**
**Department of Labor**

**and**

**The Internal Revenue Service**
**Department of the Treasury**

**In Response To**

**Their Request For Information**
**Regarding Lifetime Income Options**
**For Retirement Plan Participants**

**May 3, 2010**

# REQUEST FOR INFORMATION FROM DEPARTMENTS OF LABOR AND TREASURY

## Introduction:

As many of the products being addressed in this RFI are relatively new to the defined contribution market, IRIC thought that it would be beneficial to provide a brief description of the different product types available.

First, plan sponsors can offer either an in-plan or out-of-plan institutionally-priced lifetime-income product, and in some instances, offer both. Additionally, a lifetime-income product can be fixed or variable. Fixed products provide a guaranteed amount of income that remains unchanged and is set for life. These products are usually invested in the general account of the issuing insurance company. Variable products provide a benefit that will change over time, based on the investment performance of an underlying fund. These products frequently take the form of separate accounts. In today's market, institutionally-priced income products for defined contribution (DC) plans include:

- In-plan immediate annuities – These products provide a guaranteed lifetime income by annuitizing a participant's plan balance.
- In-plan deferred fixed income annuities – These products allow participants to purchase pieces of income annuities over time and at different interest rates and ages. At retirement, the balance is fully annuitized.
- In-plan guaranteed minimum income benefits – These products also allow individuals to purchase a guaranteed income product over time, which will be annuitized at retirement, and also include a "floor" for the guaranteed income amount. Positive investment performance of the underlying fund can increase the payout during retirement. Guaranteed minimum income benefits go by the acronym GMIBs.
- In-plan guaranteed minimum withdrawal benefits – These products allow participants to lock in a "high-water mark" value for their account at retirement, which will then be used as the benefit base for the guaranteed minimum amount of income (say five percent annually) that can be withdrawn each year for life. The guarantee remains in place even if the market value of the underlying portfolio reaches zero. Guaranteed minimum withdrawal benefits go by the acronym GMWBs and are sometimes referred to as guaranteed lifetime withdrawal benefits or GLWBs.
- Out-of-plan immediate annuity – Many plans allow individuals to roll their savings into an Individual Retirement Annuity at the point they retire. The product delivers an annuitized income for life.
- Out-of-plan immediate annuity rollover platform (shopping service) – Distribution agents have set up IRA rollover platforms that allow retiring participants to use software to access quotes from several insurance companies for comparison and purchase of immediate annuities at retirement.
- Out-of-plan guaranteed minimum withdrawal benefits – Similar to the in-plan version mentioned above, this product is an IRA rollover, with benefits commencing when the participant terminates employment and rolls over their account balance.
- Out-of-plan payout funds – These funds will pay income out over a certain period of time, such as 20 years. The funds may be structured to pay out any combination of principal, interest, or earnings over a set time or until the funds expire. The funds are not insurance products that guarantee that payments are made for life.

## 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?**

The primary advantages of lifetime income products are:

- Because the product is guaranteed for life, participants will continue to receive payments up to the point of death, e.g. they will not "outlive their assets".
- The burden for managing the income stream is significantly less than it would otherwise be.

- The type of distribution can be chosen to suit the retiree's needs, e.g. protection can also be provided for a spouse.
- Uncertainty about one's financial future causes a great deal of stress and manifests itself in reduced productivity during working years and a lower quality of life in retirement. By creating a stream of secure lifetime income, these negative impacts can be mitigated.
- When lifetime income is secured, retirees become less vulnerable to being sold an unsuitable product in the retail marketplace.
- Since they benefit from the pooling of risk, guaranteed lifetime income products will typically generate a higher amount of retirement income than self-insuring via the utilization of an appropriate withdrawal rate.

The primary disadvantages of lifetime income products are:

- Participants have reduced flexibility and control.
- Lifetime payments are more difficult to understand.
- Participants may pay a fee for a service they may never use. When it comes time for retirement and the annual/monthly payment seems small relative to the lump sum, they may end up taking a lump sum payment forfeiting any guarantee. (This is a common occurrence in defined benefit plans when a lump sum is a distribution option.)
- Depending on the type of lifetime product, individuals who annuitize their DC portfolio with a guaranteed lifetime income product and then die shortly after retirement would have left more of their retirement wealth to their beneficiaries if they had not invested in a lifetime income product.

**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?**

This question will be answered as if it is directed to the low utilization of lifetime income in defined contribution (DC) plans and IRA vehicles.

Traditionally, the discussion of low utilization was tied to the offering of immediate income annuities at the point of retirement. Indeed, according to a survey of large 401(k) plans by Hewitt Associates only 14% of DC plans offer annuities and only 1% of the covered participants actually invest in an annuity. (Source: Hewitt: Trends and Experience in 401(k) Plans 2009) IRIC feels that this is due primarily to the way the decision is presented to participants and how they make this decision, which is becoming better understood through the study of "behavioral economics".

Most rank and file workers choose a lump sum distribution because purchasing an annuity (or selecting an annuity from a DB plan) is a daunting, one-time, irrevocable decision which involves loss of control and flexibility. There is a tendency by the individual to underestimate how long they will live and overestimate their ability to effectively manage their savings as they age. Selection of a lump sum is often the "path of least resistance" and plan sponsors generally take a passive role and do not discourage it. In the short run, selecting a lump sum allows the individual to feel wealthier because they have control over a relatively large pool of assets. Furthermore, the financial advisor community generates a significant amount of their income from commissions and fees resulting from the rollover of DC assets to the retail market. In other words, local financial advice is usually encouraging the lump sum distribution.

While there is always room for innovation and improvement in the annuity market, the high incidence of retirees selecting lump sum distributions from defined contribution plans indicates the primary barrier is participant inertia and poor decision making. Yet even when inertia is not a critical factor, e.g. when DB plans offer an annuity as the default distribution option, we see a strong preference by retiring participants to choose the lump sum option.

Employers and plan sponsors are in a unique position to influence participant decisions through plan design, the strong messaging power of defaults, and providing participants with stronger guidance. The Agencies can influence the role plan sponsors take in helping their workforce make decisions that are in their own best interest by developing regulations that encourage plan sponsors to take steps that result in better outcomes. This includes support for defaults, safe harbors, and a federal program to guarantee annuities up to a maximum amount. That said, special consideration must be given for those participants with small amounts of plan balances. EBRI reported that at the end of 2008 the average 401(k) balance plan balance is approximately $125,000 for those in their 60's, so continued emphasis must also be on continued contributions throughout the accumulation years.

The Pension Protection Act is illustrative of the positive impact plan design and defaults can have on outcomes, while continuing to allow participants choice, flexibility, and control if they want it. The Agencies should build on the lessons learned from PPA to encourage better retirement outcomes for participants through an increased use of annuity distribution options. If low utilization by participants to-date is due to complexity and cost of the lifetime products being offered, these issues should be considered before a default mandate is recommended by the DOL.

**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?**

Pension plans (defined benefit, money purchase) are required to offer an annuity option, but utilization of the annuity option is extremely low if a lump sum distribution option is available.

In a defined benefit plan, the annuity is typically funded and insured by trust assets and the PBGC, unless the plan is terminated, and the liability is sold to an insurance provider. In a money purchase pension plan, the annuity is typically provided through an out-of-plan solution by purchasing an annuity from an insurer at the time the distribution option is selected.

Profit-sharing plans do not have to offer an annuity option and only about 14% of large 401(k) plans offer a traditional immediate income annuity at retirement. Within those plans only about 1% of the covered participants actually invest in an annuity

A number of new products that provide guaranteed lifetime income have been introduced in the DC marketplace as in-plan options. These include deferred fixed income annuities, guaranteed minimum withdrawal benefits (GMWBs), and guaranteed minimum income benefits (GMIBs). GMWBs and GMIBs are also occasionally available as IRA rollover products that are offered through the institutional plan relationship. Immediate annuities are also available through the institutional plan relationship as IRA rollovers and are made available from a single provider or via a "supermarket" purchasing platform which has lower commissions than comparable retail products. (Refer to the introduction for a description of these different types of products.)

Further, there continues to be product development in the IRA rollover area including the usage of asset allocation strategies with structured payments. While these are not insurance-backed products, they offer participants some of the same features of lifetime income as an in-plan offering. We expect to see these types of solutions offered as institutional products into the qualified plan arena.

**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?**

About 14% of 401(k) large plans offer an immediate income annuity option as a distribution option at retirement and only about 1% of the covered participants invest in an annuity. (Source: "The Survey Findings: Trends and Experience in 401(k) Plans", Hewitt Associates 2009). There are currently a very small number of plans (perhaps less than 100 nationwide) that offer out-of-plan immediate annuity shopping platforms and GMIBs mentioned above at the point of retirement. When this does occur, it would take the form of an IRA rollover.

With the in-plan version of deferred fixed income annuities, GMWBs, and GMIBs, the products are designed to overcome behavioral obstacles to encourage utilization. Investments are made over time, usually with each contribution, e.g. not with a lump sum. Individuals benefit from dollar cost averaging of investing and/or different interest rate environments. Individuals begin to think about their DC wealth in terms of lifetime income as opposed to a lump sum of accumulated wealth. And participants are provided some market risk protection during their accumulation phase.

The in-plan products are structured to allow for institutional pricing and fees are usually paid for income guarantees when they are provided. Deferred fixed income products embed the guarantee fee into the product and this impacts the future monthly benefit to be provided. With GMWB and GMIB products these fees are assessed as an asset based fee on the current market value similar to the other investments in the DC plan. Participants typically have the right to transfer out of the investments prior to retirement.

The products differ on the degree of guaranteed income provided and amount of flexibility and control at retirement. Deferred fixed income annuities and GMIBs will typically generate higher guaranteed lifetime income amounts and will require annuitization upon retirement. To generate the higher income and benefit from the risk-pooling provided by the insurer, participants will usually give up control of their account when they begin to generate lifetime income due to the annuitization. With the GMWB, individuals will typically will receive lower initial amounts of guaranteed lifetime income (relative to fixed income annuities or GMIBs) and maintain the ability to leave the fund at any time with their remaining market value.

**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?**

IRIC is unaware of the statistics that provide the answer to this question. Anecdotally, it appears that when lifetime income options are offered, they are almost always offered as a choice, requiring the participant to affirmatively elect the option in lieu of another form of payment. This applies to employer contributions and employee contributions.

**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?**

There are numerous types of IRA rollover products that provide lifetime income. All of these products start the benefit payments at the point of rollover. These include GMWBs, GMIBs, and immediate annuities. Other types of retail IRA products are available that provide lifetime income but are not necessarily guaranteed for life. Recently, the marketplace has seen the rollout of mutual funds that can be used to generate income over one's anticipated lifetime. These are called managed payout funds and they provide a distribution over time but do not guarantee that payments are made for life. Currently, guaranteed products can only be offered by insurance companies.

To the second part of the question, the answer is "yes". There are IRA products available that allow the participant to have portability of their DC in-plan benefit should they terminate employment and leave the DC plan. These IRA offerings typically provide the individual the right to "port" any income guarantees and rights along with market value accrued to-date to the IRA. However, the participant may forfeit the institutional pricing allowed while in the plan and be subject to higher retail fees.

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?**

A number of features can impact the cost of the retirement income product. Many of the features are designed to encourage utilization (become more attractive in the eyes of the participant) and/or provide enhanced value compared to traditional withdrawal strategies. It boils down to a trade off between the amount of monthly benefit and the cost of various features. Due to the impact in the financial markets as a result of the economic downturn, some of the benefits have been stripped down to reduce cost.

Among the features that can increase cost are:

- Inflation protection such as scheduled payment escalators or increases tied to the CPI.
- Guaranteed lifetime minimum payments that provide a future floor of income.
- Ability to pass on remaining market value at death or other form of death benefits.
- Ability to lock in a "high water mark" guarantees.
- Hedging costs incurred by the product manufacturer.
- Flexibility such as the ability to take non-scheduled payments, higher payments, or transfer monies out of the investment at any time.
- Ability to increase and lock-in higher amounts of guaranteed lifetime income due to positive market performance.
- Ability to grow guaranteed lifetime income due to guaranteed growth rates referred to as roll-ups.
- Flexible liquidation terms upon contract termination at the plan sponsor level.
- Investing in actively managed funds as opposed to indexed funds.
- Allowing participants to have higher equity allocations.

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)?**

It should be noted that a DC plan can offer an in-plan option or an out-of-plan product at the point of retirement. Both allow the participant to acquire the product as a result of the relationship with the plan sponsor. The out-of-plan rollover products offered when the participant elects to leave the plan will typically provide the product at a lower cost than a comparable retail product sold through a financial advisor.

The advantages of the in-plan option include:

- Protection during the accumulation phase.
- The ability to "dollar cost average" into different interest rate and stock market environments.
- Avoidance of spot interest rate risk at the moment of annuitization.
- Avoidance of a single major decision which is often so daunting participants avoid it.
- Lower costs than comparable retail products offered through a financial advisor due to longer time commitment and institutional pricing.
- Participants conditioned to think early on about retirement income and not building a lump sum of retirement wealth.
- Plan sponsors will be conducting some level of due diligence on the lifetime income product whereas the individual does not benefit from this protection in the retail marketplace.

The disadvantages of in-plan solutions are:

- The primary value of lifetime income products is realized only if the participant remains in the investment through retirement.
- The participant may pay fees for a guarantee they may never utilize if they liquidate the amount accumulated in the annuity vehicle before they begin receiving payments.
- The participant appreciates the benefit less because it is harder to grasp (one of the reasons defined contribution plans gained favor over defined benefit plans).
- The participant may end up with several smaller "annuity accounts" (with potentially different annuity providers) as they change jobs because contracts cannot be consolidated.
- The participant is exposed to the credit worthiness of the insurer.
- The distribution options are limited to those defined by the plan document. Participants can select from a greater array of optional forms of payments with an out-of-plan product.
- Unisex tables are required, which results in annuity purchase rates for males being more expensive than the out-of-plan option and leads to anti-selection problems. With an out-of-plan annuity, males can purchase products using sex-distinct actuarial tables, resulting in higher payments.

**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?**

From the standpoint of the plan sponsor the advantages of offering an in-plan option include:

- The ability to help plan participants with their personal retirement security including assistance with:
    1. Acquiring guaranteed lifetime income security at a reduced cost compared to the retail market.
    2. Protection from sales practices that are not in the retiring workers best interest.
    3. Ability to ease into a lifetime income investment over time which will overcome the behavioral obstacles that exist today that keep individuals out of annuity products.
    4. Providing a framework as to how much retirement income can be safely withdrawn annually from the DC portfolio without fear of running out of money.
    5. A plan to help participants secure income and reduce complicated decisions when they face the "old" phase of retirement - when they are most in need of assistance and may become a burden on their families or on society.
- The ability to screen the lifetime offerings their participants will eventually be utilizing. This can also be offered at the point of distribution with an institutionally-priced IRA offering as well.
- Being able to properly educate employees about lifetime income while they are employed. Research shows that the workplace is the place that workers prefer to learn about retirement planning. And, we believe educated employees are more likely to prepare for retirement and be able to retire when they are no longer productive at work. This in turn helps employers more effectively manage their workforce.
- With an in-plan offering, participants can benefit from pre-retirement protection, as well as dollar-cost averaging into different investment markets and interest rates. These attributes of the in-plan offering should result in more individuals being able to retire as planned. This will result in lower overall benefit and wage costs for the employer.
- With an in-plan offering, average plan costs per participant may decrease as more participants with larger balances stay in the plan for longer periods.
- If the objective of the plan sponsor is to help participants generate retirement income, the plan sponsor has a greater effect on utilization with an in-plan product. Immediate annuities have been offered for years as "point-of-distribution" options and the track record shows that individuals are attracted to the lump sum option. Financial advisors also encourage their clients to take the lump sum option since there is a monetary gain to them as they steer their clients into products and services that generate commissions and/or fees for these services. This results in low utilization of lifetime income options by the individual.

- Allowing participants to identify how much retirement income has been acquired at various points during their working years will likely increase the likelihood that participants will increase their contributions going forward, which in turn makes it easier for the employer to manage their workforce for many of the reasons cited above.
- If the in-plan option is valuable and effective, the retirement plan could become a stronger vehicle to attract and retain workforce talent.

From the standpoint of the plan sponsor, the disadvantages of offering the in-plan option include:

- The DC plan becomes more cumbersome by
    1. An increased responsibility to monitor product(s),
    2. Greater complexity with regard to changing recordkeepers and/or product providers, and
    3. Increased administration and communication burdens.
- Participants may not be as focused and engaged on the investment decision as opposed to when they are retiring. It is likely that guidance on lifetime income and investment options may be more effective at the point of distribution. Therefore, for an employer with predominately younger workers, the appreciation for the effort of including lifetime income options may be diminished.
- Similarly, unless approaches are developed to increase participant utilization of lifetime income products, a lot of work may take place without a significant payoff. Plan sponsors may question the value of adding the product to their plan.
- There can be a number of reasons that a plan sponsor is indifferent to increasing the income security of their employees. If this is the case, there are few advantages to adding an in-plan option other than the ability to have their employees retire as planned (i.e. manage their workforce) Everything else is an additional burden to the current savings plan mode of the DC plan.

Note that it is possible that an out-of-plan lifetime income vehicle could be offered to the plan participant as an immediate annuity. This avoids some of the disadvantages faced by plan sponsor relative to the in-plan solution, but this model has existed for years and has had very little attraction to, and therefore utilization by, retirees.

**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?**

IRIC strongly believes that each plan that offers a lifetime income product must allow for a full or partial investment in that vehicle. Restricting an investment to an “all or nothing” requirement will likely do more harm than good. Addressing the specific questions:

- 14% of DC plans offer an immediate income annuity at retirement. The source of the data in this survey is larger plan sponsors and a conservative assumption is that smaller plans have even fewer offerings of immediate income annuities. (Source: “Survey Findings: Trends and Experience in 401(k) Plans”, Hewitt Associates 2009)
- Although statistics are not available, we believe most of these plans do not require an “all or nothing” annuity decision and allow for partial annuitization, however, most annuity providers have minimum requirements.
- For guaranteed lifetime income products to work, each plan must allow for partial investments in these products and perhaps even liquidity during the accumulation stage of investing.
- The determination of the amounts to go into guaranteed lifetime income products is important. Participants should be encouraged to generate guaranteed lifetime income to cover projected monthly “essential” expenses.

**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?**

It is important to recognize that behavioral strategies have indeed been supported and embraced in the accumulation stage of the DC plan experience. A big accelerator of the use of these strategies (such as automatic enrollment) was the introduction of Safe Harbors in The Pension Protection Act of 2006. It is also important to realize that lifetime income products have been offered at the point of retirement (distribution) from the DC plan for over 30 years with little use. In a survey of larger 401(k) plans, Hewitt points to usage of 1% per year of those retiring who are offered an annuity. Cash balance plans also see little annuitization.

However, defaulting a participant to join a plan and start saving is quite different than defaulting a participant to a lifetime income solution. One view is that plans need to be careful to educate their employees if they are indeed defaulting their participants' money into a lifetime income vehicle. The other view is that education is likely to fail (as it has elsewhere) and there should be support for defaulting participants into lifetime income vehicles since it is in the best interest of most to put them on a path where their savings generates some amount of guaranteed lifetime retirement income, while preserving the right of the participant to opt out.

IRIC believes that plan sponsors should be able to decide whether or not they wish to default their participants into a lifetime income solution during the accumulation stage. To make this choice a realistic option to plan sponsors, further guidance, clarity, and a safe harbor is needed from the DOL. If they do plan on utilizing a lifetime income vehicle as a default, plan sponsors should be able to choose the type of product that is offered and the portion of savings directed to the lifetime income option based on their own evaluation of what is best for their plan participants. For example, plan sponsors may wish to consider the richness of the benefit, cost, liquidity, provider experience in the marketplace, product simplicity, in-plan or out-of-plan, or other factors.

IRIC further believes that the Agencies can pave the way for wider use of defaults and still allowing plan sponsors to choose. The Agencies can issue clear safe harbors that plan sponsors can follow to be comfortable making the decision to have a lifetime income product as the default option.

**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?**

IRIC does not believe all of a participant's balance should be allocated at distribution into an irrevocable annuity product that cannot be accessed for emergency needs. How much of a participant's DC balance should be allocated to a lifetime income product will depend on many factors, including the type of lifetime income product being considered, other sources of retirement income, etc.

Factors to consider include the amount of guaranteed income provided (if any), the investment mix in the lifetime income product, and the liquidity offered by the product. Participants will need guidance on how much guaranteed lifetime income they should provide themselves and a good "rule of thumb" is for them to plan on covering all essential monthly expenses such as housing, medical care, and food with a guaranteed amount of lifetime income provided through a combination of sources such as Social Security, pensions, and a guaranteed lifetime income product. With this approach, the individual is assured a minimum standard of living that will keep them out of poverty due to poor investment performance in their portfolio or living longer than expected.

Every participant's situation will be different and although rules of thumb can be beneficial when planning far into the future, plan sponsors should be encouraged to educate and provide planning tools to pre-retirees so that they may understand how to incorporate lifetime income vehicles and traditional investments into their retirement income planning process. This is explored further in our response to questions 22-24.

The Agencies may wish to consider mandating a change to the statutory requirements for information provided at the time of distribution and retirement to include a base level disclosure of the benefits and disadvantages to staying in-plan versus rolling assets out of plan to an IRA and include the concepts of secure lifetime income. The critical point being that retiring participants should understand the pros and cons to maintaining access to institutionally priced products within their DC plan.

**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?**

IRIC believes that a lifetime income option should not be mandated either as a default or as a requirement to reside as an option in DC plans. However, the Agencies should consider encouraging plan sponsors to look at these options and the potential value that could be brought to participants. Under this consideration, plan sponsors could decide whether to offer the guaranteed lifetime income option in-plan during the accumulation stage through distribution or just at the point of distribution. For those plan sponsors who wish to adopt these solutions as defaults, the Agencies should provide clarity, guidance, and safe harbors to encourage adoption.

Due to the conservative nature of the investment, the Agencies should consider how a fixed deferred income annuity can be used as a default for a portion of contributions, such as the employer match. Further, although many (including IRIC) understand that the regulations state that adding an income guarantee does not preclude an investment from qualifying as a QDIA, the perception among some plan sponsors, consultants, and recordkeepers is that this may not be true. As such, we suggest that the Agencies provide guidance and clarity that reinforces that GMWBs and GMIBs meet the current QDIA regulations.

Since plan sponsors may wish to offer lifetime income products as defaults, a clear safe harbor should be issued to clarify what protections exist for plan sponsors for defaults to lifetime income products that are initially invested in during the "in-plan" accumulation phase. Currently, plan sponsors are reluctant to adopt in-plan retirement income products due to the uncertainty and perceived additional liability they will assume by adopting those products.

Beyond those plan requirements, though, participants should be given flexibility to make their own investment decisions. For example, a participant should be allowed to apply the guaranteed lifetime income option to some of his account, none of his account or all of his account.

Furthermore, the lifetime income option should, beyond the fact that it is guaranteed by a financial institution that is regulated for this purpose, be defined in the broadest possible terms--to allow for and encourage future innovations.

**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?**

Based on IRIC's "in the field work" with plans sponsors on this subject, we consistently hear the following themes:

1) Many plan sponsors do not feel this is their issue to address. Once the participant has left employment of the firm many plan sponsors feel the obligation to the participant ends at that time. This is magnified with the number of participants that change jobs or companies that have gone through downsizing. As a result many plan sponsors have not spent the time to become educated on this part of the market.

2) Given the market turbulence over the last two years most plan sponsors have been paralyzed and have not made any big changes. This affects several areas, not just retirement income. Most plan sponsors have focused on cutting costs and managing other critical needs within the company and have not been focused on retirement plans.

3) Many plan sponsors do not know where to start in evaluating the products, ask even the most basic questions, or find objective information. The general feeling among sponsors is the products in the market are complex. This is compounded since many consultants/advisors are not knowledgeable about the offerings in the market.

4) Many plan sponsors that are familiar with the retirement income market feel the market cycle is still early. The products will continue to evolve and they see no reason to be an "early adopter".

5) Plan sponsors also have concerns about counter party risk and the guarantee being backed by a single insurer. This concern was magnified during the market turbulence of 2008. There is much confusion as to what, if any coverage is provided for in-plan guaranteed lifetime income products by the state guaranty associations. A clear and direct explanation of the coverage provided could provide the biggest push towards a widespread adoption of these institutionally-priced products. Another option to consider would be to nationalize the coverage such as is done with the FDIC and the PBGC

6) Lack of participant demand is another area that discourages interest by some plan sponsors. While many surveys indicate that participants are interested in having a retirement income option, when one is offered, the actual use of the products is quite low. Plan sponsors do not want to use their time implementing a lifetime income option if ultimately participants do not use it.

7) There are several impediments under ERISA and the Internal Revenue Code. The first is the fiduciary responsibility requirement for the selection and monitoring of lifetime income products. Plan sponsors are concerned that they do not have the ability to select insurance companies that will be in existence 30, 40 or even 50 years from now, when the benefits are paid. In other words, plan sponsors do not understand that the prudent man rule requires that they evaluate the provider of the guarantee based on today's circumstances. Instead, there appears to be a belief that plan sponsors are responsible for the financial stability of financial service institutions well into the future. Therefore, the duties of fiduciaries with regard to guaranteed lifetime income options need to be clarified.

   As a part of that clarification, the Department of Labor should re-visit its safe harbor annuity provisions under Reg. §2550.404a-4. First, the Department needs to clarify that the current regulation applies to guaranteed lifetime income options beyond traditional fixed annuities with the alternative being to create new regulations for GMWB products. (The new GMWB products are more similar to insurance policies than they are to annuities, but some may view them as annuities.) In addition, the regulation could provide greater guidance on evaluating costs and other issues.

8) Portability is also a significant fiduciary issue. Plan sponsors are concerned because a significant portion of the providers and recordkeepers today will not support annuities, GMWBs, and similar products. As a result, plan sponsors are concerned that, if they do not have universal portability opportunities upon the change of recordkeepers, they will be breaching their fiduciary duties. Clarification on that issue is needed.

   As an alternative to clarification, or perhaps in addition to it, the Internal Revenue Code could be amended to permit qualified plans to make distributions upon changes of providers where a participant might otherwise lose a feature under the plan. For example, if a 55-year-old participant had paid several year's worth of premiums for a guaranteed lifetime income option, and then the plan sponsor switched to another provider that would not maintain that feature, the participant should be allowed to take a distribution and roll over into an IRA (i.e., the potential loss of the feature would be a distributable event). Rollover IRAs are generally available for these guaranteed products.

9) Finally, the qualified joint and survivor annuity rules (QJSA) impose a substantial barrier to the near-term expansion of lifetime income guarantees (to the extent that they are subject to those rules). As 401(k) plans have grown in popularity, the vast majority of plan documents have been drafted without annuity provisions. As a result, in order to add lifetime income options (if they are subject to the QJSA rules, that is, if they are deemed to be life annuities), plan sponsors would have to amend their plans to include annuity provisions and to include the QJSA and QPSA rules. That would obviously impose a significant expense and administrative burden on plan sponsors nationally--and would particularly impact small plan sponsors.

   In that regard, the IRS has recently issued three private letter rulings that have created concern, and even confusion, in the 401(k) community. Those private letter rulings found that, in some cases, non-traditional annuity lifetime income guarantees (like GMWBs) would be treated as life annuities by the IRS, but that in other cases they would not. The impact of those private letter rulings on the QJSA rule is not clear on the face of the rulings, although it appears that in many cases the GMWBs would not be considered to be life annuities for QJSA purposes. Clarification is needed in order for lifetime income guarantees to be accepted in the marketplace.

**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?**

IRIC believes that it is premature to look at adding more complex products to the discussion at this time.

**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?**

Statistically, women outlive men, exposing women to greater longevity risk. The shift from DB pension plans to DC plans in the private sector, where the lump-sum option is now widely accepted as the default, has put more women at risk of poverty in their advanced years. The QJSA rules (and protection for spouses) that were put in place for retirement plans have been eliminated in most DC plans as income annuities have been eliminated as distribution options.

It is also important to note that guaranteed lifetime income provided by traditional DB plans not only ensures that income will not be outlived but it eliminates the responsibility for retirees of having to manage their retirement assets to generate income. The ability of retirees to manage their retirement income strategy declines as they age.

Further, lower socio-economic retirees often do not have the wealth to pay for financial advice, the investment savvy to manage investments, nor the ability to self-insure a lump sum distribution through retirement. The Agencies may wish to consider how lower socio-economic groups can benefit from the “automation” of generating retirement income that guaranteed lifetime vehicles can offer. This group of Americans is at great risk of outliving their savings, resulting in old-age poverty.

## PARTICIPANT EDUCATION:

**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 provides it, and when and how is it provided to them?**

Because plan sponsors and fiduciaries will have prudently selected, and continue to monitor the particular guaranteed lifetime income option and provider of that option, participants can focus on questions of how much, when, and what features. However, these products are complex and it is important participants understand key issues.

The provider of the lifetime income product needs to offer specific education about the product being offered.

Accordingly, the Agencies may wish to consider requiring that each participant be provided fundamental information such as:

- Material that clearly identifies that this is a lifetime decision for the participant as most products in this category are providing benefits in the form of future lifetime income. For guaranteed lifetime income products, the material should disclose which insurer is providing the guarantee as well as provide information on the financial stability of that insurer.
- If the product does not offer a guarantee of principal or a guaranteed return on principal, this should be made clear. Further, if there is a guaranteed annual increase of the benefit base, this information should be presented in a manner so that it is clear to the participant that this is a guaranteed increase of the benefit base as opposed to a guaranteed return on principal. Material should also clearly identify what portability the individual will have in the future if he severs employment from the plan sponsor. In other words, can the individual preserve income guarantees by remaining in the plan or rolling over assets and guarantees to an IRA?

- An explanation of the nature and features of the guarantee, including any conditions and/or restrictions. (This would include a description of the guaranteed amount, either as a dollar amount or percentage, for example, 5% of the “benefit base”--which could vary over time. Alternatively, for a fixed annuity, the benefit could be described as approximately 7% of the account balance at the time of purchase, or as an annual or monthly dollar amount.) There should be at least one uniform method by which all providers would need to express the guarantee. For example, that could be an annual percentage of the account value or benefit base, depending on the product. In that regard, the difference between a benefit base and the account balance would need to be explained.
- The cost of the guarantee for lifetime income, including clearly identifying whether the fees being paid are explicit or implicit. The maximum fee should be disclosed as well, including information as to whether this fee applies to only future assets invested or all of the assets currently in the product as well as future assets.
- Any restrictions in accessing the market value of the lifetime income investment either in the accumulation phase or in the future payout phase should be clearly disclosed. This includes any restrictions resulting from ineligible withdrawals. This would also include any additional restrictions on participant elections such as loans, withdrawals, transfers resulting from an investment in the lifetime income product.

The final part of the question inquires about the current information provided to participants in regards to securing lifetime income. We have found that there is no standard approach to providing this information to participants. The information will vary based on plan sponsor preferences, the type of products provided, and the ability and desire of the recordkeeper to provide this information. Answers to questions 21-23 provide IRIC’s suggestions to how this information should be provided in the future.

**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?**

Generally speaking, plan sponsors appear to understand that they can pay for the provision of information and education about plan investments and services from plan assets. However, it is not clear that fiduciaries can spend plan assets in order to educate or provide information to participants about investments and services that are not provided by the plan; in other words, there is a significant issue about whether plans can use plan assets to provide participants with education about broad retirement issues or information about services and investments that are outside a plan.

In any event, while some plan sponsors may appreciate these issues and have access to legal advice, many do not. As a result, clarity on any of the issues addressed by this RFI would be helpful to at least some plan sponsors. However, it is critical that the guidance be specific and unambiguous--and that it be clear that alternative approaches may be acceptable.

**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?**

The general knowledge among most plan sponsors for guaranteed lifetime income products is very limited at this point. Only a handful of plan sponsors have taken the time to become familiar with the legal issues around lifetime income. The concerns about education on lifetime income options are similar to those for investment options, but are of greater concern because of the relative newness of these features and services and the long time frames involved for the guarantees. As a result, the patterns of communication and education are less established and are currently being developed. There needs to be continued education for the plan sponsors to help them be better equipped to address the legal issues.

It would be helpful to either expand Interpretive Bulletin 96-1 or to provide separate guidance relative to lifetime income. Many service providers and consultants are reluctant to serve as fiduciaries and, as a result, the growth and popularity of annuities and other lifetime income guarantees would likely be slowed if providers and consultants felt that they were obligated to serve as fiduciaries for providing information and education.

Similar to IB 96-1, the guidance could provide that information about life expectancies, historic investment returns, various simulation of withdrawals over time periods, the impact of various withdrawal rates, longevity risk, and market sequence risk (among other issues) was "education."

Further, most participant-directed plans intend to comply with 404(c) and as such, participants have a variety of asset classes from which to choose. But if a plan offers only one lifetime income guarantee, the discussion of that guarantee should be defined as education, rather than investment advice--similar to the use of asset allocation models, with specific investments in the models, under IB 96-1.

**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?**

The answer to this question is similar to the preceding question. At the least, the Agencies may wish to encourage plan sponsors to provide participants with information about reasonable estimates of the lifetime income that their accounts can purchase. In addition, plan sponsors should be encouraged to provide participants with the opportunity to use a calculator to consider issues such as other assets that they or their spouse may have (or may contemplate receiving), the impact of delaying retirement, and so on. While these encouragements may be suggested to plan sponsors, as a practical matter they will be satisfied by providers for all but the largest plans (which may be administered internally). In fact, many providers already offer both of those services, that is, the ability to project retirement income and the calculators that participants can use to make additional calculations. However, the Agencies should encourage that any retirement income calculator provided to participants by the plan be able to accurately reflect the retirement guarantees provided under the plan options.

IRIC also recommends that the DOL consider making available a generic calculator that can provide illustrations of future retirement income amounts.

In addition, the Agencies may wish to encourage plan sponsors to educate participants about the advantages and disadvantages of lifetime guarantees, for example, the situations in which participants could, if they do not have a guarantee, run out of money because of longevity risk or risks attributable to the sequence of market returns.

It is important that information be provided to participants when they enroll in the plan, as they participate in the plan, and especially at retirement (or other distributable events). Those multiple touch points are important because participants need to be thinking about the need for retirement income and the value of guarantees as they participate in the plan. Otherwise, for many participants, it is likely that they will be overwhelmed at retirement by the introduction of new materials and issues. When participants are overwhelmed, they often take the simplest option, which is cash.

- For example, plans that have adopted lifetime income products have been known to change their education programs to incorporate wider discussion of the risks retirees face and how lifetime income products can help mitigate those risks.
- Quarterly statements have been enhanced to include a projected future monthly retirement income amount in addition to the current market value of the account.
- On-line planning tools have been enhanced to help participants plan for their future expected monthly expenses and to gauge where they are in relation to their goals by incorporating Social Security, investments, and lifetime income products.

## DISCLOSING THE INCOME STREAM THAT CAN BE PROVIDED FROM AN 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?**

Individual benefit statements should, at least annually, present the participant's account balance as a projected lifetime income stream of payments beginning at the participant's Social Security retirement age.

Unfortunately, many plan sponsors and participants continue to see 401(k) plans as “savings” plans, rather than as “retirement” plans. In other words, they focus on the amount that they have saved, or accumulated, without realizing that it should be viewed as a stream of income payments during retirement. The projections would help both plan sponsors and participants understand the retirement income issues and the adequacy of the account balances for that purpose. In turn, that would likely lead to improvements in plan design and operation, as well as increases in participant deferrals (or other compensating participant behavior).

IRIC strongly encourages the DOL to issue not only clarifying guidance on this issue but a clear safe harbor. We strongly believe that safe harbors are the most effective way to encourage plan sponsors to adopt these changes to their plans.

**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?**

IRIC recommends the projections on the statement should:

- Project what the current account value would buy in monthly income at Social Security retirement age assuming the participant made no further additions to principal, received an appropriate real rate of return, and:
- Project a second balance that assumes the participant keeps contributing at the current level, the employer continues to make the company match at its present rate, with an appropriate assumed real rate of growth on the participant’s investments, through Social Security retirement age.
- Projections should be in today’s dollars.
- Projections, with the caveat noted below, should be done as a single life annuity.

In addition, the Department of Labor should provide a website which has a calculator for these purposes. The Department of Labor could work with various industry groups, as it did with the initial fee disclosure forms, to develop such a calculator using well-considered practices and research. If the Department provided that calculator, it would provide a strong influence in establishing accepted standards for projecting and communicating retirement income needs, similar to the impact the Social Security Administration had when it introduced annual benefit statements with projections. Further, there would be substantial savings to 401(k) plans and participants.

So as not to cause confusion at the participant level, plan sponsors should also be allowed to use the income projection methodology of the in-plan retirement income product if one is offered. The Agencies may wish to encourage a footnote to the straight life annuity projections mentioned above to indicate that providing a similar benefit to a spouse for life (i.e. 100% joint and survivor annuity) would reduce the guaranteed income amount by approximately 16%. Further, plan sponsors should be encouraged to provide additional information and projections using reasonable assumptions and disclosures. It would be helpful for the Department of Labor to provide a regulatory safe harbor for the range of assumptions that plan sponsors may use for projecting these future income amounts. See answer to Question 23.

We emphasize that the payments should be expressed in the form of monthly amounts, since the typical participant is used to being compensated on a monthly basis and to paying his bills on a monthly basis. In other words, the normal financial cycle for most workers, and most retirees, is monthly.

Also, the monthly income should be projected as current dollars because, if the information is provided in future inflated dollars, participants will have an inaccurate sense of wealth.

Since plan sponsors in most instances do not have access to employees’ complete wage history, the Social Security Retirement Estimator calculators are more accurate in projecting future Social Security benefits. The Agencies should encourage plan sponsors to provide links on their websites to these calculators.

IRIC strongly encourages the DOL to issue not only clarifying guidance on this issue but clear safe harbors. We strongly believe that safe harbors are the most effective way to enable plan sponsors to adopt these changes to their plans. See answer to Question 23.

**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?**

The DOL should establish several safe harbors plan sponsors may use for projecting retirement income:

- The assumptions used by the DOL calculator (recommended in response to question 22); or
- The assumptions used by the retirement income option included in the plan (if one is offered); or
- The assumptions used by the defined benefit plan (if the plan sponsor also offers); or
- A set of assumptions which, in the aggregate, produce reasonable results and follow the principals established under FASB and GAAP as applied to defined benefit pension plans under ERISA.

Participants should be given disclosures about the material assumptions and any potential weaknesses related to the assumptions. Thus, participants should be told that the projections of lifetime income payments are estimates and can vary based on a number of factors, such as date of retirement, interest rates in the future, earnings on the underlying investments, form of payment, and so on.

In developing the safe harbor, the Department should make it flexible to allow for evolving products and circumstances. The benefit of the safe harbor is (and should be explained in the preamble to the regulation) that the Department of Labor clearly intends that there be a fiduciary safe harbor (and protection for service providers) so long as assumptions are used that are reasonable under the circumstances. Further, either the preamble or the regulation, or both, should specify that there is a broad range of reasonableness and that the standard is to be applied at the time that the assumptions were made, regardless of future developments. The safe harbor would also protect employers from liability in the event the amounts that are illustrated exceed the amount of benefit that actually accrues at the point of retirement.

The point of the safe harbors should clearly be to encourage plan sponsors to provide these future projections. The Agencies should encourage the practice that any ancillary projections provided to participants via calculators or other means should be consistent across the plan to avoid participant confusion and frustration.

**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?**

Plan sponsors, fiduciaries and providers should be encouraged to provide participants with information concerning replacement ratios and income needed in retirement. However, IRIC believes that this information should not be required to be provided on the benefit statement, but allowed to be made available through other means where the participant initiates the discussion and is able to provide inputs as needed. The Agencies should consider that recordkeepers do not always have full salary information in their data systems to provide accurate projections.

Further, spousal information is unlikely to be available for any plan so replacement ratios should clearly be disclosed as representing one life.

Just as the Social Security Administration has created a standard for projecting Social Security benefits when they began providing annual statements, the DOL calculator mentioned in response to Questions 22 and 23 could provide a strong influence in establishing a standard for a general replacement ratio threshold. The team developing the application should be tasked with researching what the appropriate replacement ratio should be, along with establishing other assumptions used in the calculations.

IRIC strongly encourages the DOL to issue a clear safe harbor that covers employers putting projected income replacement ratio information on either the benefit statement or in an advice tool. We strongly believe that safe harbors are the most effective way to enable plan sponsors to adopt these changes to their plans. In effect, a regulatory safe harbor should be created for any replacement ratios that are based on reputable academic and/or industry research. Further, the safe harbor should explicitly apply to a standardized threshold for all participants in a plan, without regard to their individual circumstances (such as their earning levels).

The primary concern is the need to balance the value of providing participants with an initial expectation for a replacement ratio, while recognizing plan sponsors do not have access to the information needed to provide a meaningful estimate for a participant based on their unique facts and circumstances. There is a concern among fiduciaries and providers that providing a generalized replacement ratio exposes them to additional risk and fiduciary challenges because it may not be appropriate for a specific participant based on their specific situation. Establishment of a safe harbor would address this concern.

## 401(K) AND OTHER PLAN QUALIFICATION RULES:

**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?**

The primary barriers in the qualification rules are found in the QJSA provisions. That occurs for two reasons. First, it is not clear whether certain product structures, such as GMWBs, are treated as life annuities for plan purposes generally and for QJSA purposes specifically. To the extent that they are, it imposes a substantial cost and administrative barrier on the growth in popularity of these guarantees. That is because almost all 401(k) plan documents now provide for only lump sum distributions (and perhaps installment payments over a term certain). Stated slightly differently, there are relatively few 401(k) plan documents that currently provide for annuity payments and for satisfaction of the QJSA rules.

The primary reasons for this are it is expensive and administratively burdensome to satisfy the QJSA rules and few participants and/or their spouses have taken advantage of the protections provided by the QJSA rules. Therefore, while on paper the QJSA rules provide protections to participants and their spouses, the reality is that they do not. Plan sponsors have drafted their documents to avoid those rules because they provide little benefit, but incur additional expenses and impose an administrative burden.

The second reason is similar. Since few plans provide for annuities (and, therefore, few contain the qualification provisions required by the QJSA rules), virtually all 401(k) plans would need to be amended if annuities were offered or if GMWBs were treated as annuities. That would obviously result in additional costs and impose an administrative burden (especially for small plans), and would likely increase the number of plans out of compliance --- especially small plans --- and facing disqualifying defects.

To clarify these issues, the Department of Treasury should re-evaluate the question of whether GMWBs are or are not to be considered life annuities and whether the QJSA regulations apply. For instance, are GMWBs considered life annuities if, and when, they are distributed at or before the exhaustion of the participants' account (and thus before the guarantor is obligated to make payments)? (At the time of distribution, the GMWB only has prospective financial value, that is, it provides for payments if the participant exhausts all of his rollover IRA assets at some point in the future.) That would be consistent with the analysis in Phase I of Private Letter Ruling 200951039. (The language in the three private letter rulings issued by the IRS on this subject is confusing. There is a need for clarification on a number of issues, such as distinguishing between the investments, which belonged to the participant or investor, and the guarantees, which are separate from the investments and which can be surrendered or terminated at any time by the cessation of the payment of the underlying fees or premiums.) If the Department of Treasury clarifies that GMWBs are not life annuities for QJSA purposes, the acceptance of those lifetime guarantees would be much greater, and certainly would occur much faster.

With regard to traditional and deferred fixed income annuities, the QJSA issue is somewhat more complex in the sense that the application of the statute is clear. As a result, in order to simplify the process and reduce the cost, legislation would be needed to remove this barrier toward greater acceptance of these types of retirement income solutions.

Another issue exists in regards to portability of these products at the plan level should the plan sponsor wish to change providers to a recordkeeper that cannot support the current lifetime income product. To encourage the adoption of these products, the Agencies should create legislation allowing for a distributable event (to an IRA for instance) if the plan is no longer going to offer the product. In this way, plan participants would feel more comfortable enrolling in these products and plan sponsors would feel more comfortable making them available.

**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?**

To foster the use of lifetime income products, the Agencies should recognize that greater adoption will occur if the administrative hurdles are reduced. This includes the need to make plan amendments. Compliance costs need to be minimal as well. Unfortunately, any increase in administrative requirements or a substantial increase in administrative costs will impede the adoption of these products. We can look to history as a guide as many DC plans have dropped immediate annuities options due to the QJSA administration required.

Specifically, there is a need for clarity regarding the life annuity definition and, therefore, of whether the qualified joint and survivor annuity rules apply to situations that do not involve traditional income annuities. That would include, for example, guarantees (GMWBs) that are "wrapped" around investments and which operate more in the nature of insurance (i.e., would only pay off if the insured event--the depletion of the account--occurs). See response to Question 25.

Further, to lower cost and the administrative burden, the Agencies should consider permitting an electronic signature as a way to meet QJSA requirements.

**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?**

Greater clarity will indeed reduce the uncertainty for deferred income annuities and guaranteed minimum income benefits. However, as discussed in response to Questions 25 and 26, administrative requirements and cost must be kept minimal to encourage widespread adoption of guaranteed lifetime income products.

**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?**

While the RMD issue is a topic that should be addressed, it is currently not a reason that will impact a plan sponsor's interest or lack of interest in lifetime income products. The administrative issues around the RMD question are a nuance but would not prevent a plan sponsor from adding to the plan if they have interest.

That said, clarity from the Agencies is welcome. Specifically, the Agencies should look at clarifying whether longevity insurance products can be utilized with qualified plan assets. Clarity would also be beneficial around whether the actuarial present value of the income guarantee within a GMWB should be included in the value of the assets for RMD calculation purposes. Most GMWBs on the market today are "RMD-friendly" in that they will allow for a higher amount than the current guaranteed minimum withdrawal amount to be withdrawn to satisfy an RMD requirement. This would not be deemed an "excess withdrawal" and would not reduce future guaranteed income withdrawal amounts. Note in-plan deferred income annuities already have the RMD exemption applied due to the annuitization that occurs at the point of retirement.

**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?**

IRIC has not seen this activity widely used outside of governmental plans where 403(b) and 457(b) assets are used to purchase service credit under the defined benefit plan. When we have seen it, participants of defined benefit plans are allowed to transfer some or all of their defined contribution balances into the DB plan in exchange for monthly annuity payments from the DB plan. All the usual optional forms of payment are available (life only, J&S, etc) plus an "Installment Refund" option. The Installment Refund option will, in the event of the death of the participant, pay a monthly amount to a named beneficiary in certain circumstances. If the participant dies before he has received payments totaling his original lump sum transferred into the DB plan, his beneficiary will continue to receive monthly payments until the total payments made from the DB plan (with respect to the amount transferred into the plan) equal the original amount transferred into the plan.

This type of arrangement effectively allows participants to purchase lifetime annuities from the DB plan at "wholesale prices." There are no commissions or loads, etc. connected with the transaction. The DB plan assumes both investment risk and mortality risk from the participant. The conversion factors take into account a rate of return very close to the return expected to be earned by the plan's funding policy over the long term and the additional mortality risk is pooled with the entire plan population.

This is a particularly valuable benefit, especially for plans that have frozen benefits at some point in time. It allows participants to try to make up the difference in a cost effective manner. Further, the benefits are protected by the PBGC up to certain limits.

IRIC believes utilization is low when this is offered and we do not believe that plan sponsors should be required to offer this feature as it may further discourage sponsorship of defined benefit plans. However, plan sponsors should be encouraged to offer and promote this option if both a DB and DC plan are offered. But it should be the plan sponsor's choice to add this option.

## SELECTION OF ANNUITY PROVIDERS:

**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?**

In the small- and mid-market for 401(k) plans, plan sponsors seldom, if ever, use traditional annuities as an option for benefit distributions. As a result, fiduciaries are generally not well versed on the provisions of the annuity safe harbor or of its implications.

To the extent that plans are using GMWB-type features as a guarantee of lifetime income, it is not clear to many of the plan fiduciaries (and their advisers) that the regulatory safe harbor for annuities is applicable.

Further, as a general comment, the regulatory safe harbor would be more effective (and, therefore, more valuable) if it were more specific in its guidance and offered a step-by-step approach. There is a need for clarification and for additional safe harbors concerning the selection and monitoring of guarantee lifetime options (other than traditional annuities). In this vein, additional examples of the appropriate information for fiduciary consideration would be helpful.

To the extent that guidance can be given which is specific and which provides plan sponsors with a high degree of confidence that they have complied with the regulatory safe harbor, it would be valuable to the 401(k) community and would promote the usage of lifetime income guarantees. In addition, the Agencies should consider providing general comments that can address not only products that available today, but future product innovations that are not insurance-based.

**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?**

As indicated in a response to question #30, there is a need for greater clarity and, preferably, for a step-by-step approach for fiduciaries. This step-by-step approach has worked well for 404(c) analysis and this "checklist" approach, we believe, will allow plan sponsors to have more confidence in their decisions and will lead to greater widespread lifetime income product adoption rates.

Importantly, there is a need for clarity that other insured, or guaranteed, features benefit from the annuity safe harbor or, alternatively, are provided with their own safe harbor. That would apply, for example, to guaranteed minimum income benefits, deferred income annuities, and guaranteed minimum withdrawal benefit-type arrangements.

For both income annuities and GMWBs, there is need for additional information about the selection of the insurer (or the provider of the guarantee). Many plan sponsors, and their fiduciaries, are concerned that they cannot predict the viability of the insurance company in the distant future, say, 30, 40 or even 50 years from now. While the regulatory safe harbor generally addresses that issue, there is a need for greater clarity and specificity. Also, the preamble should provide additional examples. It should be made clear that fiduciaries have no responsibility for the outcome in the future, if they engaged in a prudent process at the time of selection (and based on the information that was generally available at the time of the selection). It would be helpful to have additional statements of the specific type of information that should be looked in selecting a provider of a lifetime income guarantee.

The fiduciary safe harbor should also be modified to make clear that plan sponsors and their fiduciaries may rely on publicly available information, without the need to do detailed research and analysis of the type that an industry specialist would do. In addition, a plan sponsor/fiduciary should be able to rely on that publicly available information, as well as information that's generally available for the public, unless he has an actual reason to doubt the validity of the information or the competence, integrity or responsibility of the persons providing the information. (See for example, FR-11 A & A in Interpretive Bulleting 75-8.)

With regard to cost, the regulatory safe harbor is clear that the cost should be determined, at least partially, based on the guarantee and the administrative services. However, there needs to be additional guidance. Specifically, the Department should state, either in a preamble or in the regulation, that the cost of competitive and comparable products is a critical determinant of the reasonableness of the cost to a given plan while also taking into account the differences and features of the products being compared.

Finally, there is a need to address the issue of portability. While there is a growing number of providers and recordkeepers who will accept (or recordkeep) the guarantees and deferred income annuities offered through other providers, the practice is not universal. Many plan sponsors, and their fiduciaries, are concerned that they are violating their fiduciary duties by selecting a provider for a long-term option (such as deferred income annuities or lifetime income guarantees) without portability to substantially all other providers/recordkeepers. It should be made clear that (i) so long as there are a reasonable number of other providers who will recordkeep the guaranteed product (or who will cooperate with the prior recordkeeper or product provider to maintain the lifetime income guarantee in the plan), the fiduciaries will have fulfilled their responsibilities under ERISA and/or, alternatively, (ii) so long as there are reasonable opportunities to obtain similar (or competitive) products from other successor providers, the fiduciaries have not breached their duties under ERISA.

Alternatively, or in conjunction with that guidance, the Internal Revenue Code could be amended to provide for a distributable event for affected participants where a valuable feature would be lost by a participant upon a change to a subsequent provider. (As a more limited alternative, the distributable event could be limited to participants who have met a certain minimum age requirement, and whom, therefore, are most likely to be affected by the change.) With that change, participants who have lifetime guarantees and/or traditional annuities in their plan could distribute those investments and guarantees, in the case of GMWBs, to rollover IRAs or, in the case of annuities, could take distributions of deferred annuities.

Since plan sponsors can, under current law, amend their plans to permit distributions for any event at age 59½, this change would provide material protections for participants, but with little risk of abuse.

**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) 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.**

The regulatory safe harbor for annuities (or a similar regulatory safe harbor) should be extended to all lifetime income guarantees that are underwritten by qualifying financial services institutions (which would ordinarily be insurance companies). A broad safe harbor would facilitate the development and acceptance of new alternatives, both now and in the years ahead. To do otherwise would favor one form over another, which would be an inappropriate intrusion (or preference) by the government in the marketplace.

## ERISA SECTION 404(c):

**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?**

We interpret this question to inquire about deferred fixed income annuities that are acquired over time within the DC plan and then annuitized at retirement. When offered, participants can accumulate units in deferred fixed income annuities in their 401(k) or other defined contribution accounts. During the accumulation period, the annuity accumulations are, from an investment perspective, analogous to stable value investments. In that regard, participants can transfer in and out of their 401(k) investments in the deferred income annuities, however a surrender charge or market value adjustment may apply.

With regards to deferred fixed income annuities, the advantages are that:

- The participant locks in at the time of purchase a future guaranteed retirement income amount. So there is no uncertainty.
- The individual is able to gauge what their monthly or annual retirement income gap is likely to be.
- Purchases over time allow for purchases at varying interest rates and this avoids “at retirement” spot interest rate risk.
- Annuitization at retirement of deferred fixed income annuities is the most efficient way to maximize lifetime income due to the risk-pooling involved. Since the majority of participants are behind in their savings goals and do not have access to DB plans, this option maximizes their retirement income payment.

The disadvantages of deferred fixed income annuities include:

- No exposure to the equity markets.
- Participants cede control of their retirement assets when they start taking payments due to the annuitization requirement, which causes many not to annuitize.
- Fees are not easily transparent as they are built into the product. Fees include administration fees as well as fees for assumptions related to mortality, interest and discount rates, and investment management
- A surrender charge or market value adjustment may apply when transferring out of the fund.

**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?**

IRIC sees a growing minority of ERISA 404(c) plans providing guaranteed lifetime income through variable annuity contracts such as guaranteed minimum withdrawal benefits and guaranteed minimum income benefits. Participants are informed of: any applicable fees; the nature and method of determining benefit guarantees; restrictions relating to transfers between the product and other investment alternatives; and the effect of any such transfer on the benefit guarantees.

The protections afforded by 404(c) would be valuable to fiduciaries relative to participants who affirmatively directed that their account's investments include a guaranteed lifetime income feature. If plan sponsors and fiduciaries had a clear roadmap for obtaining the fiduciary protections afforded by 404(c) relative to guaranteed lifetime income benefits, that would allow them to adopt the new features and guarantees with less concerns, real or not, about any fiduciary risks. As a result, participant use of these products would increase.

With regard to guaranteed lifetime income products, the advantages to the participants are that:

- Participants are assured that they will not outlive their money during retirement.
- Participants usually have the option to provide lifetime income protection to a spouse.
- Products introduced in recent years look and feel like mutual funds during the accumulation stage of the worker's life.

With regard to guaranteed lifetime income, the disadvantages to the participants are that:

- A participant may pay fees for insurance over a number of years but may cancel that coverage by transferring prior to retirement and not fully realize the benefit of the insurance being provided.
- Participants will be restricted as to how to they can invest the underlying funds.
- The product being offered may be too complicated for a participant to understand.

## <u>QUALIFIED DEFAULT INVESTMENT ALTERNATIVES:</u>

**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?**

The most common use of guarantees in a QDIA context is where plan fiduciaries select a target date fund or as the QDIA for the plan, together with a lifetime income guarantee. There are two variations of that arrangement. The first is where the guarantee attaches immediately (including the fee for the guarantee) on the defaulted account of a participant (subject, in some cases, to a minimum series of fee payments, e.g., five years). The second is where the accounts of defaulted participants are placed in the QDIA, but the guarantee and the fee do not begin until the participant has attained a specific age, for example, 10 years prior to the date on the target date fund. Although fixed annuity and GMWB products are available in the market using this approach, they are not yet being used with any frequency as QDIAs.

While the preamble and the QDIA regulation provide a basis for reasonably concluding that an insurance feature may be part of a qualified default investment alternative, it would be helpful if the 404(c)(5) regulation clearly referenced lifetime guarantees in conjunction with qualifying QDIA investments. That would eliminate any possibility of interpretations to the contrary. As an example, there appears to be differences of opinion in the benefits community on whether GMWB products qualify as QDIAs so further clarification would be helpful. Alternatively, the Department of Labor could, through other means (for example, an advisory opinion) clarify its intentions. To encourage more widespread adoption of these products, plan sponsors will need more clarification and guidelines from the DOL on QDIA rules.

## COMMENTS REGARDING ECONOMIC ANALYSES, REGULATORY FLEXIBILITY ACT, AND PAPERWORK REDUCTION ACT:

### 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.

We see the following benefits for a plan sponsor in offering an in-plan option:

- Contributions can be invested in a retirement income product over a period of time, resulting in less behavioral resistance compared to the “at-retirement” purchase of a lifetime income product.
- Contributions invested over time in a retirement income product have the ability to realize the benefits of dollar cost averaging.
- There is mitigation of investment risk prior to and through retirement by using income guarantees.
- Participants could have the ability to “test drive” investment in a retirement income product subject to certain fees, prior to retirement.
- Improved retirement planning for a plan sponsor’s workforce as participants would not be inclined to work beyond their effective working years as a result of a market declines and uncertainty of future retirement income.
- If plan administrative costs are offset by revenue from investment products, keeping the terminated participant balances (usually the larger balances) in the plan through the use of an institutionally-priced lifetime income product will help reduce the plan’s administrative costs.

The costs to the plan sponsor are as follows:

- The time and expense of understanding these complicated products, which likely involves engaging experts to help evaluate the options and implement.
- Recordkeeping is another cost. Currently there are a limited number of recordkeeping platforms that can accommodate these products. This translates into higher costs and limited portability for now.
- If participants with smaller balances remain in the plan after termination, the plan recordkeeping costs will increase.

### 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?

Due to limited scale, there are limited offerings available in the market for small plans.

**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?**

Making a lifetime income product the default form of benefit payment at distribution is not enough alone to significantly impact employee contribution amounts. The key to increasing employee contributions is to provide frequent retirement income projections so that participants begin thinking about their defined contribution wealth as future amounts of retirement income.

**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?**

No comments as this information is not readily available.