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VIA Federal eRulemaking Portal

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

Attention: Lifetime Income RFI

Dear Sir or Madam:

I am writing on behalf of Lincoln National Corporation[1] and its affiliates, in the aggregate commonly known as Lincoln Financial Group, to provide comments for the Request for Information Regarding Lifetime Income Options for Participants and Beneficiaries in Retirement Plans ("RFI"), Department of Labor RIN 1210-AB33. We appreciate the opportunity to provide information we hope is helpful in determining how the U.S. Department of Labor ("DOL") and the U.S. Department of the Treasury ("Treasury") (hereinafter together, the "Agencies") may assist Americans to better secure their retirements through the use of assets accumulated in their defined contribution plans[2].

We will follow the structure of the RFI and will repeat some of the headings and follow the numbering framework for the questions found in the RFI. Those headings and the questions are repeated below in italics, followed by our responses.

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?

Response: The main advantage of lifetime annuity payments is the assurance that the participant cannot outlive the payments and thereby run out of money. Lifetime annuity payment options shift the mortality and investment risk to the insurer and provide peace of

[1] For nearly 50 years, The Lincoln National Life Insurance Company has served the retirement plan market. Through a selection of product offerings, Lincoln Financial Group serves over 25,000 corporate, government and non-profit employers, helping them provide retirement benefits to their 1.3 million American employees. Lincoln Financial Group is known in the industry as an income innovator, especially for its patented approach to lifetime income.
[2] Unless our responses specifically provide otherwise, they should be read to include Internal Revenue Code Section 403(b) and 457(b) government plans.

mind to the participant as a result. Lifetime annuity payments may also protect the participant from the temptation to spend the assets in an accelerated manner.

There are a number of perceived or real disadvantages to taking a lifetime annuity income, all of which can be reduced or eliminated by proper design choices. One disadvantage is the risk of insurer insolvency. This risk can be reduced by diversifying among two or more insurers. State guarantee associations also mitigate this risk.

Some participants may perceive a disadvantage in "wasting" their nest egg by annuitizing and dying early before many payments have been received. In such a case, a participant may be concerned that they would be left with nothing to leave their heirs. This concern can be addressed by selecting an annuity benefit with a refund or guarantee feature, although such an approach comes at the price of a reduced lifetime annuity payment.

Another disadvantage is the timing risk associated with starting the annuity payments. A participant may start payments when interest rates used in the benefit calculation are at a low point. This risk can be mitigated somewhat by a strategy of purchasing the annuity payments in pieces over several years in a form of dollar cost averaging.

Inflation can be a disadvantage since the income payments will be paid out over a number of years. This inflation risk can be addressed with a variable annuity income stream or a fixed annuity income stream with inflation increases built in.

Perhaps the biggest disadvantage cited against annuitization is the lack of flexibility in converting an accumulated retirement plan balance to income. Annuitization is typically irrevocable and participants worry about their inability to tap the account if needed in an emergency. Lincoln Financial Group has addressed this concern with its unique, patented i4LIFE® Advantage[3] feature which gives the annuitant significant flexibility during a chosen access period.

2. Currently the vast majority of individuals who have the option of receiving a lump sum distribution or ad hoc periodic payments from their retirement plan or IRA choose to do so and do not select a lifetime income option. What explains the low usage rate of lifetime income arrangements? Is it the result of a market failure or other factors (e.g., cost, complexity of products, adverse selection, poor decision-making by consumers, desire for flexibility to respond to unexpected financial needs, counterparty risk of seller insolvency, etc.)? Are there steps that the Agencies could or should take to overcome at least some of the concerns that keep plan participants from requesting or electing lifetime income?

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[3] i4LIFE®, a patented distribution method available on variable annuity products, offers lifetime income with access to the account value. The lifetime income is a variable annuity payment with the potential to grow with the investment; however, the income payment is protected by a guaranteed minimum payment of 75% of the initial payment. The guaranteed minimum payment may also grow with a rise in subsequent income payments. The unique feature of i4LIFE® is the access period. During the access period, a participant or annuitant has access to their account balance, as well as many other rights not normally associated with an annuity.

Response: There are several reasons why participants elect to receive a lump sum distribution or to take *ad hoc* periodic distributions from their retirement plan instead of selecting a lifetime income option. These factors include:

a) The general perception, whether valid or not, that annuities are more costly than mutual funds. This perception can become an obstacle that prevents an investor from taking the time to learn the true benefits of converting an accumulated retirement nest egg into a guaranteed lifetime income,
b) The complexity of annuity products, although we believe that lifetime income options available within defined contribution plans generally are not complex and not a significant factor in the low usage,
c) The desire for flexibility to respond to unexpected financial needs is a major factor in the low usage of annuities for lifetime income. Investors generally understand lifetime annuities to be irrevocable, inflexible and inaccessible, with the insurance company keeping any assets left at death. However, insurers have developed many innovative new products in the last decade that should alleviate these concerns,
d) Poor decision making by consumers, which directly relates to the lack of materials to educate participants on the benefits of a guaranteed lifetime income,
e) Perceived risk of insolvency of the insurer isn't typically a factor in the low usage of lifetime income annuities as highly rated insurers are usually involved. However, having a federal guarantee similar to the FDIC would likely eliminate any concerns that do impact the usage,
f) Lifetime income options are not generally promoted by plan sponsors or record keepers even when such options are automatically available when an annuity is used by the plan as the funding vehicle,
g) Many participants desire to make a clean break from their previous employer and move assets to an IRA,
h) Advisors who provide education and guidance to participants may be reluctant to recommend such options because they generally eliminate the ability of the advisor to continue managing the assets, and
i) Unisex rates for in-plan lifetime annuities are likely a factor in low usage. Participants are likely aware that males can receive higher lifetime benefits through sex-distinct rates in an Individual Retirement Annuity than an in-plan unisex lifetime annuity required by law. In-plan unisex lifetime annuity payouts are usually based on 100% female or a 50/50 blended rate due to the expectation that all males will roll out of the plan to receive a higher sex-distinct male payout in an IRA annuity leaving only female participants who will receive no less of a benefit in the plan versus out of the plan.

Educating participants on the risks of outliving their retirement assets and providing a better understanding of what level of retirement income their retirement asset will actually provide will be important elements of creating greater interest in lifetime income guarantees. However, as long as unisex rates for an in-plan annuity payout are required by law, it will be unsuitable for male participants with shorter life expectancies to stay in the plan and take an annuity option when they may roll their account balance to an IRA annuity and receive higher gender-distinct income.

3. What types of lifetime income are currently available to participants directly from plans (in-plan options[4]), 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?

Response: Defined benefit plans have traditionally offered lifetime income to participants by paying benefits out of the trust on a pay-as-you-go basis or by purchasing a lifetime income annuity on behalf of the participant. The lifetime income payments can be either single life or joint lives and can be with or without a period certain feature in either case.

Defined contribution plans that offer fixed or variable deferred annuities as options during the accumulation period automatically have lifetime annuity options available as settlement options under the annuity contract. Participants seldom exercise these annuity rights, however, and frequently take a lump sum distribution that is rolled over to an IRA or take systematic withdrawals from their account balance.

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?

Response: Historically, lifetime income has been provided to retiring defined contribution plan participants by converting the accumulated defined contribution account balance at retirement to a lifetime income annuity. This option is still available in almost all defined contribution plans funded with a deferred annuity, although usage is infrequent.

Some plans are starting to offer defined contribution plan participants the option to purchase guaranteed lifetime income on an incremental basis during the deferral period. In some cases, participants purchase a small amount of guaranteed lifetime income starting at retirement with each periodic contribution to the defined contribution plan. In other cases, participants choose guaranteed living benefit (GLB) riders, which guarantee a future minimum account value or other benefit amount that is used to calculate the guaranteed withdrawal amounts.

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?

Response: One service provider we are aware of offers an employer sponsored annuity as an investment option with employer contributions. With this product a target date fund is used, but instead of allocating a portion of the contributions to a conservative fixed income investment, an allocation would instead go to a deferred fixed annuity. Longevity risk is addressed through the embedded fixed-deferred annuity. Also, the deferred fixed annuity

[4] For our purposes here, an "in-plan option" means any lifetime income distribution option provided through the employer's plan, including an option initially elected by the plan participant at the end of his or her career with that employer.

is held at the fund / plan level rather than at the individual participant level, allowing a low-cost product. Since the insurer does not have to keep track of participant-level details which is normally the case, the product can be offered at a reasonable cost of 50 basis points which includes both the cost of the fund / plan annuity as well as the investment management fee of the other investments in the target date fund. Like other target date funds, the service provider allocates a larger portion of the portfolio into the annuity as participants approach their retirement date / age of 65.

We do not think employers / sponsors have or will adopt a product where only one source of money (employer match or non-elective contributions) can be used to purchase a guarantee or annuity because:

a) **Many defined contribution plans have all sources of money follow the same investment election,**
b) **Allocating only employer contributions to the annuity fund and allowing other contributions to be self directed would cause that employer to forgo 404(c) protection for the plan assets purchased with employer contributions,**
c) **Some employers and most employees do not view their employer contributions differently than deferrals in terms of the benefit afforded to the workforce, and**
d) **A separate election adds unnecessary complication to the enrollment process and recordkeeping system.**

Another provider offers an in-plan guarantee and lifetime annuity offering that enables plan sponsors to "default" (similar to an automatic enrollment / negative election) participants at age 50 into the guarantee. However, very few employers have adopted this "automatic" approach and defaulted employees into this guaranteed option.[5]

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[6]*), 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?*

Response: Individuals who roll their assets out-of-plan can access a variety of lifetime income options within an IRA. Investors seeking guarantees that they will not outlive their assets can invest qualified assets in either fixed or variable IRA annuities with living benefits that include guaranteed fixed income or guaranteed minimum withdrawal amounts for life. All versions of annuities (fixed, variable, immediate, deferred) can generally be used within an IRA.

[5] Retirement Services Roundtable – Income Products Research Paper 2010

[6] For our purposes here, an "out-of-plan option" means any lifetime income distribution option provided through an IRA or nonqualified financial vehicle purchased with assets distributed to the participant from the plan.

Annuity purchase rates are specific to the purchased contract and therefore will likely be different between the plan contract and the individual contract. If favorable annuity rates are available in-plan, participants can exercise the lifetime income option under the plan and would not have to roll over to an IRA to gain access to favorable annuity purchase rates.

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?

Response: Product features that have a significant impact, positive or negative, on the cost of providing lifetime income are:

a) **Mix of investment in equities and fixed income/bond funds,**
b) **Income or withdrawal rate as a percent of the account balance,**
c) **Flexibility to accelerate income and fully withdraw account balance,**
d) **Ability to reset and increase lifetime income guarantee,**
e) **Time until lifetime income begins,**
f) **Ability to raise cost in the future, and**
g) **Availability of death benefits**

The cost to the participant can come in two forms. One form is the actual basis point assessed against the participant's account balance to purchase the income guarantee. The other form is in a lower level of lifetime income provided or investment flexibility.

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)?

Response: In-plan advantages might include:

a) **For women, the use of unisex mortality tables, required by federal law for employment based plans, may provide a greater benefit than a comparable out-of-plan life annuity,**
b) **Familiar investments where the in-plan benefit is purchased at the end of employment with the plan sponsor,**
c) **A participant can begin purchasing lifetime income benefits early in their careers and allow inertia to work to the participant's advantage,**
d) **Lower cost due to group pricing, including no or lower commissions, which could result in higher monthly income for participants than comparable out-of-plan options,**
e) **A plan fiduciary will choose, and periodically review, lifetime income options which should relieve participants of doing as extensive due diligence as might be required for an out-of-plan option,**

f) The availability of such a form of distribution in the plan will make it more likely that participants will choose it, and
g) Timing risk is addressed by the use dollar cost/interest rate averaging where purchases are made over a number of working years.

In-plan disadvantages might include:

a) For men, the use of unisex mortality tables, required by federal law for employment based plans, may provide a lower benefit than a comparable out-of-plan life annuity that would not likely be offset by the use of group mortality rates. We believe that this is a significant deterrent to the development of widely used in-plan lifetime income options,
b) In-plan options may not be portable. There are substantial administrative challenges if the plan sponsor decides to replace the current plan service provider/record keeper. Many record keepers do not have the ability to administer and maintain records with respect to lifetime income products that are provided by another service provider/record keeper,
c) The significant additional administrative burdens related to spousal consent requirements will cause many defined contribution plan sponsors to choose not to offer in-plan lifetime income options,
d) Participants changing their mind about the desirability of the in-plan option may cause them to incur expenses for guarantees they may never use,
e) The number of in-plan products offered may be limited due to the plan sponsor's willingness to develop their use in its plan, and
f) Participants may accumulate several small benefits from different employers' plans offered by different service providers with no readily available means of consolidating those benefits.

Out-of-plan advantages may include:

a) Use of gender distinct mortality tables will provide greater lifetime annuity benefits to men than to women,
b) Much greater choice of products, forms of distribution, investment options and service providers than a plan sponsor can make available in its plan,
c) Individuals will have greater access to financial advisors to assist them in selection of an out-of-plan lifetime income option,
d) A participant might be able to roll over a portion of his plan account to a product of the plan's service provider without certain fees and restrictions, and
e) Ability to cut all ties with employer,

Out-of-plan disadvantages may include:

a) Use of gender distinct mortality tables will provide lesser benefits for women then for men,
b) Potentially higher retail pricing when provided outside of a plan as opposed to institutional pricing when provided in-plan,

c) **Individuals are less likely to purchase lifetime income products out of plan incrementally, increasing the risk that such lifetime income benefits are more expensive when purchased, and**
d) **The complexity of lifetime income distribution products discourages decision making where plans may provide assistance through the selections it made.**

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?

Response: An advantage to the plan sponsor is that it will be able to help its employees better prepare for retirement and to more readily attract good candidates for available positions and make long-term employees confident enough in their financial security to retire. The plan sponsor might have more bargaining power with an insurer given the aggregate assets in the plan compared to the lesser amount in a participant's individual account available to the participant after receiving the plan distribution.

In addition, a plan sponsor with the vendors it selects will have a much better opportunity to educate plan participants throughout their employment career with respect to some in-plan lifetime income options as compared to post-employment out-of-plan options.

The biggest disadvantage is the additional burden on a plan sponsor to choose an insurer to provide an in-plan option for guaranteed lifetime income. See our response to Question 31 for an analogous explanation of the disincentive to plan sponsors to provide out-of-plan lifetime income options.

In-plan lifetime income options are viewed unfavorably by some plan sponsors and plan participants because in-plan lifetime income options are not usually available and readily understood in plans not funded with annuities and because of some such products inherent complexity. As a result, generally there is not a strong demand for them in the current marketplace.

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?

Response: Our understanding is that most plans that offer lifetime annuities as a form of payout / distribution offer such distributions on all the assets available for benefit or a portion of the assets. However, for a variety of reasons, many plan sponsors do not offer a life annuity and for those that do, participants generally do not ask for their payout (or a portion of their payout) in the form of a life annuity. Lincoln Financial Group does not

believe that offering a partial life annuity option would by itself change the low adoption rates we see today by plan participants.

Today's retirees will receive only part of their retirement security through their defined contribution plan balance. Other sources of security will come from:

a) **Appreciation in home values,**
b) **Other personal savings ,**
c) **IRA accounts,**
d) **Defined benefit plan,**
e) **Social Security,**
f) **Inheritance or anticipated inheritance, and**
g) **Other insurance policies.**

As a result, many participants will aggregate their assets on or near retirement and formulate a financial plan at that time. Participants generally consolidate assets (distribution out of the defined contribution plan and into an IRA or other savings vehicle) and then review and adjust asset allocation, investments in annuities, insurance policies, etc. Because of this typical process, partial annuity options in defined contribution plans will not make a measurable difference in whether participants select a lifetime annuity option.

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?

Response: We are not aware of any plans that are using such default or automatic arrangements. While using an automatic or default income provision would clearly encourage more lifetime income, we do not think that plan sponsors or participants will welcome such a mandate. An alternate, more palatable approach would be to encourage plan sponsors as a best practice to offer a lifetime income option and education on the benefits of lifetime income, but not require the participant to elect the option.

While it does not appear that plan sponsors are using such behavioral strategies to any extent to encourage lifetime income from defined contribution plans, assuming that the Agencies provide rules to encourage lifetime income payments from defined contribution plans, 401(k) and ERISA rules should be modified to provide clear protection to plan sponsors who include such options and education in their plans. In particular, inclusion of

lifetime income distribution options within QDIAs would appear to be particularly promising. Use of automatic enrollment has increased plan participation where used. We believe that permitting QDIA investments to include lifetime income features would increase such features' use.

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?

Response: Each participant will have his or her own specific reasons for choosing what portion of their account balance to annuitize, but the factors that a participant should considered in making this decision are tolerance for risk, size of account balance, individual health, other assets, spouse or partner needs, and level of guaranteed income needed. At a minimum, basic living expenses should be covered through a guaranteed lifetime income.

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?

Response: No.

Many plans and plan sponsors do not currently offer lifetime annuities. Many sponsors and participants have grown accustomed to retirement security and retirement planning as an individual responsibility – not the on-going responsibility of the employer long after the participant is no longer employed. Requiring a plan to offer an annuity or lifetime income option would be costly and as we have seen, simply making the option available has not caused a significant adoption of the payout option. Plan administration issues including plan termination complications, 5500 reporting, required amendments, additional administration, additional forms, additional notices, and notarized spousal consent rules would all be costly new requirements that would not measurably increase retirement security under a required / mandatory approach. In money purchase plans, a lifetime annuity is the required / default / first option. Even in this environment, most participants choose to get a notarized spousal consent in order to receive their distribution in another form or to roll it over to an IRA.

Despite the above challenges of requiring annuitization or requiring that plan sponsors offer some lifetime annuity option, Lincoln Financial Group believes that living benefits and lifetime income options are becoming increasingly important to participants, sponsors, providers and policy makers in Washington. As such, retirement security and retirement income will continue to be the focus of articles, product development efforts and advertising. Accordingly, Lincoln Financial Group believes that annuities and lifetime income products will become a more common plan and investment design feature inside defined contribution plans and will become a best practice in the industry much the same way as daily valuation or Web based transactions are now considered best practices. We encourage the Agencies to issue guidance that would facilitate the adoption of such options

so that plan sponsors would view these products as prudent and sound from a fiduciary perspective. The sound fiduciary practice and best practice status, however, should not come at the cost of complicated and costly fiduciary evaluation processes and standards which could act to thwart their adoption and growth.

Lincoln Financial Group would also support efforts to encourage individuals to include lifetime income as part of their individual retirement planning. This could be accomplished through:

a) Defined contribution plan statements that reflect projected balances and the projected annual income of that balance through an annuity,
b) Tax incentives to purchase annuity payout options (especially for lower income individuals),
c) Financial literacy programs, and
d) Encouragement and incentives to rollover defined contribution plan balances to an IRA where distributions from the IRA are in the form of a life annuity or guaranteed lifetime income or other type of lifetime payout option such as installment payments over the participant's life expectancy.

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?

Response: We think that the impediments are primarily a lack of understanding of the importance of including such an option in a plan along with the difficulties and uncertainties of doing so currently. We also believe that such lack of understanding accounts for the low participant demand. Plan sponsors do not appear to want to take on any additional responsibility, and the accompanying liability, related to choosing an annuity provider since the current ERISA rules do not provide objective criteria that plan sponsors may use in making such a choice. In addition, 401(k) qualification rules related to required minimum distributions ("RMD") and qualified joint and survivor annuities ("QJSA") provide unwanted complexities and uncertainties on how certain lifetime income methods should be handled. Adjustments to the RMD rules to permit the exclusion from the RMD calculation of actuarially determined lifetime income and "longevity insurance" financial products would be helpful. QJSA rules add an additional complexity since many believe that simply having an annuity available in a defined contribution plan causes the entire plan and all distributions, loans and other transactions to be subject to the QJSA requirements. That is not a correct interpretation of the law and this matter needs to be clarified in order to encourage plan sponsors to provide lifetime income options in their plans by understanding that the application of the overly complicated QJSA and QPSA rules will only apply to the actual election of a "life annuity." QPSA rules should be eliminated in this context and QJSA rules should only apply at the point that the participant's decision will become irrevocable as described elsewhere herein.

The cost of lifetime income products such as annuities is perceived to be high due, in part, to their relatively low use and other factors such as adverse selection. We do not believe

that those are significant factors in the cost of annuities. In fact, we do not believe that annuities are expensive when viewed from the perspective of the guarantees that annuities provide and restrictions that need be placed on income withdrawal strategies to try to ensure that those assets will last throughout a plan participant's life. The use of guaranteed lifetime income distribution annuities can be increased by the Agencies through education; providing incentives, including regulatory safe harbors and tax incentives; and regulation encouraging the choice of lifetime income annuity distribution options in defined contribution plans.

State insurance law will apply to annuities needed to pay guaranteed lifetime income from defined contribution plans. While that state law will add some additional complexity, that burden will be more than offset by the added protection such state law will provide to plan participants using those products, including the possible availability of state insurance guarantee funds.

During the current economic crisis, we have seen increased concern from plan sponsors about Lincoln Financial Group's financial health. While not specifically related to lifetime income distribution options, that concern certainly included those matters. We do not believe that concern about the solvency of the guarantor of the lifetime income guarantee is currently a major factor impeding the use of guaranteed lifetime income benefits since the actual use of lifetime income distribution options in defined contribution plans was negligible prior to the current crisis. As described elsewhere in our RFI responses, that is particularly relevant to a company such as ours since almost all of our products and services to retirement plans include an annuity which, by definition, permits distribution in the form of lifetime income, i.e., annuitization. Specific concerns with solvency related to the ability to continue to pay lifetime income over a long period of time may become a factor as more plan sponsors and participants give such benefits serious consideration. There is some movement in the insurance industry to spread the risk across multiple insurers for a single plan.

While product complexity is an issue, we believe that impediment can be overcome with sufficient education.

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?

Response: Combining annuities with another product like long-term care leverages one dollar into two benefits. That dollar can be used for future lifetime income or future long-term care expenses. These two benefits are <u>generally</u> offsetting risks. The average length of all long-term care claims is 2.04 years[7]. The number of combination long-term care annuities currently is fairly limited, although with the specific provisions of the Pension Protection Act of 2006 becoming effective January 1, 2010, we expect to see a number of new combination products introduced in the near future. We do not expect to see

[7] Society of Actuaries, LONG TERM CARE EXPERIENCE COMMITTEE, INTERCOMPANY STUDY, 1984 – 2004

combination products involving qualified plan annuities or IRAs, however, because of the limitations in Code section 7702B(e)(4).

We are not aware of any annuity products that are linked to reverse mortgages. A variable annuity would likely not be suitable in combination with reverse mortgages. A fixed annuity that guarantees principal may be suitable under certain circumstances.

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?

Response: For retirement plans, annuities are required to be actuarially priced under unisex pricing assumptions. In other words, men and women of the same age would receive the same annuity payout with their defined contribution balance if their plan offered an "in-plan" annuity option. However, if both a man and a woman of the same age rolled their assets over to an individual retirement annuity, i.e., an IRA, the woman would receive a lower payment due to the longer life expectancy of women. Thus, some advisors / planners recommend that women take an annuity payout "in-plan" (if offered) and men to take an annuity payout outside the plan in an individual annuity product. This will generally result in the highest possible payout for men and women that seek guaranteed income from their defined contribution plan balance.

By having participants take their distribution as a rollover to an individual annuity, the annuities can be more equitably priced based on the known mortality risks of different groups.

To the extent the Agencies want to encourage annuitization from defined contribution plans, it would be essential to get the federal legislative relief necessary in order to more appropriately price defined contribution annuities based on true mortality factors between male and female annuitants.

Participant Education

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

17. What information (e.g., fees, risks, etc.) do plan participants need to make informed decisions regarding whether to select lifetime income or other arrangements designed to provide a stream of income after retirement? When and how (i.e., in what form) should it be provided? What information currently is provided to participants, who typically provides it, and when and how is it provided to them?

Response: Participants should be given a full description of the types of lifetime income options available, along with comparisons of other options available, including systematic

withdrawals. Advantages or disadvantages of the various options, as well as the fees associated with each option, should be discussed. For each available option, there should also be a full description of the option, how long it is guaranteed, what happens at death, and guidance on suitability of the various available options taking into account other sources of retirement income such as defined benefit pension and Social Security. The disclosure should be provided in writing far enough in advance of the election date for thorough information analysis and the option to meet with an advisor to review the options.

Provision of this information currently is inconsistent and lacking uniformity and usually comes from the annuity provider or the advisor.

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?

Response: While guidance on this issue would be helpful to encourage plan sponsors to consider such distribution options, we do not think it necessary. It seems clear to us that plan sponsors may use plan assets to provide such information, even information related to out-of-plan lifetime income options. This assumes that the determination to use plan assets to provide such information is made by a plan fiduciary in the exercise of its fiduciary obligation and in the manner appropriate for a fiduciary to make such a determination.

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?

Response: The primary concern is that such education could be determined to be investment advice for which the plan sponsor or one of its product or service providers could be determined to be a fiduciary. Such a fiduciary status could then lead to one of those parties, not otherwise a fiduciary, to have engaged in a prohibited transaction or other fiduciary breach. The Agencies can provide guidance to make clear that such education will not be considered investment advice. Specifically, the DOL could do this by modifying its Interpretive Bulletin 96-1 or including such a concept in its announced review of the regulations under the definition of a fiduciary under ERISA concerning investment advice.

As noted in our response to Question 18 above, some plan sponsors are concerned about using plan assets to provide education about out-of-plan lifetime income options. Again, it would be helpful to clarify that doing so can be an appropriate use of plan assets, as determined by an appropriate plan fiduciary. Such clarification could be provided in Interpretive Bulletin 96-1 or other appropriate guidance.

A decision to eliminate a lifetime income option from a plan could subject plan sponsors to claims of fiduciary breach if a plan sponsor makes a fiduciary determination to eliminate such option. A participant could face the prospect of losing a guarantee that he or she had

been paying for and which may be providing a benefit at the time of elimination. The plan participant may not have the option to retain the guarantee via a direct rollover since changing plan providers does not constitute a distributable event. Such a situation would place the sponsor in an untenable position. The Agencies should remedy this barrier to in-plan lifetime income options by making clear that changing providers resulting in the loss of a lifetime income option previously selected by a participant will not result in a fiduciary breach. This could be addressed through an expansion of the annuity distribution safe harbor provided in DOL Reg. § 2550.404a-4 as described elsewhere in our responses, clarifying that as long as the decision to select a lifetime income option product was prudent at the time it was made, plan fiduciaries will not be held liable in the event the plan fiduciary prudently decides to eliminate that particular lifetime income option or if the financial institution backing the product is unable to fulfill its obligation to pay promised benefits in the future. In addition, tax rules related to direct rollovers to IRAs should be modified to permit a plan to make a direct rollover of a participant's balance in a lifetime income option to an IRA to permit the preservation of the income guarantee accumulated in that option, if such guarantee would otherwise be lost due to a switch in providers.

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?

Response: Plans should be encouraged as a best practice to provide educational information about the advantages and disadvantages of lifetime income products or lifetime annuities. To protect the plan sponsor there should be a standard disclosure/education document approved by the DOL. Plan sponsors could provide the approved document to satisfy their education objectives without concern about liability (see response to Question 19 above).

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

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

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

Response: Individual benefit statements should be provided to participants to show a projected lifetime income. The retirement income projection should not be mandated but made available as a best practice. The projection should be provided annually at a minimum.

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?*

Response: To keep things simple, the projected benefit should reflect:

a) **both no additional contributions and contributions at the current rate,**
b) **benefits starting at the Social Security full benefit age, and**
c) **single life monthly income payments.**

In addition, participants should have access to a website or other source of information to model different benefit options and deferral rates on the same basis.

The DOL should provide standard methodology to ensure that providers do not mislead or attract business on the basis of unrealistic projections. Standardized disclosure documents would also help.

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?

Response: All providers should be required to use mandated assumptions. Specifically, a standard annuity payout rate should be required as well as a standard growth assumption for the account balance.

All assumptions and appropriate language about limitations and cautionary language should be required for everyone to see.

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?

Response: The individual benefit statement should not include an income replacement ratio. However, the educational materials should contain an explanation of the income replacement ratio, how to calculate it, and how to use it for planning purposes.

401(k) and Other Plan Qualification Rules

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

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

Response: We believe that there are a number of defined contribution plan qualification rules that affect plan sponsors' and participants' interest in lifetime income benefits.

The required minimum distribution ("RMD") requirements found in section 401(a)(9) of the Internal Revenue Code (the "Code") and sections 1.401(a)(9)-5 and 1.401(a)(9)-6 of the regulations help ensure that the tax-free growth afforded retirement vehicles is ultimately taxed by preventing extended deferral beyond age 70 ½ or certain other events. However, the RMD rules are not written in a way that adequately covers the flexibility of lifetime income options (other than traditional annuitization).

The Qualified Joint and Survivor Annuity ("QJSA") and Qualified Preretirement Survivor Annuity ("QPSA") requirements of section 401(a)(11) protect the non-participant spouse's interest in a retirement plan by requiring spousal consent for benefit elections, plan distributions and other actions. Though the rules serve an important policy objective, they are often seen by plan sponsors and investment providers as burdensome and restrictive. We believe that lifetime income options are well suited to promote QJSA/QPSA objectives, and clarifying the rules as they apply to lifetime income options, particularly how the rules affect options where the funding vehicle is a deferred annuity contract, will enhance the protection of the rules as well as the benefits of lifetime income options.

The section 401(a)(31) rollover requirements are intended to ensure that a participant's benefits are "portable," but the requirements leave some questions unanswered with respect to in-plan lifetime income vehicles. A primary question is whether an annuitized contract can be transferred out of the plan into another retirement income vehicle as a tax-free rollover transfer. Distributions from the annuitized contract are treated as RMD payments under the rule of section 1.401(a)(9)-6 of the regulations, and the regulations do not specify any method for treating any amount other than the entire payment as the RMD amount.

As a result, the portability rules relating to an annuitized benefit are not as well defined as those relating to a deferred (or non-annuity) benefit because the rollover rules would currently prevent the tax-free transfer of annuity payments.[8] In such a case, presumably

[8] Section 402(c)(4)(B) provides that RMD amounts are not "eligible rollover distributions," preventing the tax-free transfer of any amount paid from the annuitized contract to another qualified plan or IRA.

the underlying contract could be transferred to a new plan or IRA arrangement. However, the current rules do not address this issue. Future guidance should address this concern, and should provide rules to determine when the transfer of an annuitized contract will satisfy the rollover rules.

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?

Response: We believe that in-plan lifetime income options work well with the existing QJSA rules that apply to annuitized contracts. In-plan lifetime income options are perfectly suited to provide the guaranteed income stream in the form of annuity payments that the QJSA rules contemplate. However, the existing QJSA (as well as the QPSA) rules do not adequately explain how the rules apply to contracts that have not been annuitized (i.e. contracts that are in the deferral phase).

Specifically, the QJSA/QPSA rules found at section 401(a)(11) of the Code, as well as section 1.401(a)-20, Q&A-3 and 4, should be modified to provide that the rules do not apply to a participant's selection of an in-plan lifetime income option that, at the time of selection, includes a deferral period or other periodic payment option that includes characteristics that are inconsistent with the election of a life annuity. For example, if the participant has the ability to start and stop periodic income payments, to make withdrawals from an account balance or to surrender the contract and receive a surrender value, we believe that the participant has not yet elected a life annuity because such abilities are inconsistent with the concept of an irrevocable election.

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?

Response: Yes, further guidance in this area should clarify the application of the QJSA rules prior to the required beginning date and/or annuity starting date.[9] Under current law, it is not clear whether the QJSA rules apply at the time that a participant elects to invest in an in-plan lifetime income vehicle, or at the time when the participant actually elects to receive the lifetime income payments from the plan.

Under the current law and existing guidance that interprets the law, it is not clear when the IRS will determine that a participant has elected a life annuity as provided in section 401(a)(11). Specifically, we requested and received a private letter ruling[10] that discusses the application of the QJSA/QPSA rules to a qualified annuity contract. In that ruling, the IRS concedes that certain aspects of the product that apply prior to the annuity starting date are "inconsistent with the election of a life annuity." Specifically, the participant

[9] Treas. Reg. section 1.401(a)(9)-6, Q&A 10 provides that the annuity starting date will be treated as the required beginning date in the event that the participant receives payments that satisfy section 401(a)(9)(A)(ii) and such payments begin prior to the applicable required beginning date.
[10] PLR 200951039.

retained certain abilities, as provided below, following the commencement of periodic income payments but prior to the annuity starting date:

- **a) The ability to start and stop periodic income payments,**
- **b) The ability to pay additional premiums,**
- **c) The ability to make withdrawals from an account balance,**
- **d) The ability to receive a surrender value on surrender of the contract, and**
- **e) The ability to change a named joint annuitant or the annuity distribution option.**

Despite these facts, the IRS concluded that the election to begin the pre-annuitization periodic income payments constituted the election of a life annuity to which the QJSA/QPSA requirements applied. It appears from the language of the ruling that the IRS was concerned with the fact that the participant might make only one election over the life of the product, specifically the initial election to receive periodic payments prior to the annuity starting date, and not make an additional election at the annuity starting date. The language of the ruling describes the initial benefit election as "an election to receive a future benefit in the form of a life annuity, preceded by a distribution of a benefit not in the form of a life annuity." However, this conclusion ignores the fact that the participant could elect to withdraw the entire account balance following the initial election, since in actuality the participant has not at that time irrevocably elected a life annuity.

The impact of the IRS ruling in PLR 200951039 is broad in that it potentially subjects many routine participant decisions, such as whether to take a plan distribution or to change existing investment elections, to the QJSA/QPSA rules.

Guidance that clarifies that the QJSA/QPSA rules apply only after the actual, irrevocable election of a life annuity will avoid the concerns expressed above, but will not reduce the existing spousal protections afforded by the rules. For example, a non-participant spouse would, at very least, be in the same position that he or she would otherwise be with respect to a non-annuitized retirement account under such a rule. Further, such a rule could enhance a non-participant spouse's protection by encouraging the participant spouse to invest plan funds in lifetime income options.

In addition, to the extent that any further guidance clarifies that the QJSA requirements apply only when the participant actually elects lifetime income payments from the plan, such guidance should also specifically provide that an election to take RMD payments under the "individual account rules" is not an election to which the QJSA rules apply.

The RMD regulations provide that an annuity contract that has not yet been annuitized is subject to the RMD rules applicable to individual account plans.[11] A participant can take distributions from a contract, in the form of RMD payments or other non-annuity distributions, prior to the required beginning date. These distributions do affect the

[11] Treas. Reg. section 1.401(a)(9)-6, Q&A 12 states that "the required minimum distribution for any year with respect to [the deferred contract] is determined under §1.401(a)(9)-5 rather than this section."

participant's account balance, but because the distributions occur prior to the annuity contract's annuity starting date, additional plan contributions and investment gains can add to the value of the contract at the same time. These distributions do not represent an irrevocable life annuity election, as the participant can generally stop taking them or annuitize the contract at any time.

As a result, future guidance should provide that systematic non-annuity distributions or RMD withdrawals under account rules should not trigger the QJSA requirements.

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?

Response: We believe that the existing RMD rules are an impediment to sponsors offering in-plan lifetime income options because the rules related to annuity contracts[12] are unclear and difficult to apply in certain areas.

The RMD requirements that apply to annuity payout options are found in Treas. Reg. section 1.401(a)(9)-6. The regulation provides that if the contract provides for annuity payments that meet the requirements of the section, such annuity payments will satisfy the section 401(a)(9) RMD requirements. However, the regulation does not explain whether an annuity payout option could produce an annual annuity payment amount that exceeded the RMD calculated under section 401(a)(9). In other words, a participant who annuitizes his or her account will receive an annuity distribution stream made up entirely of RMDs, seemingly without the ability to take any distributions from the account that are not treated as RMD amounts. Such a participant would not, it seems, have the ability to roll over any amount from the contract following the annuity starting date.[13] This limitation puts lifetime income options at a disadvantage as compared to other non-annuity options, because under the RMD rules applicable to such options[14] it is clear that a participant can withdraw amounts from an account that do not constitute RMD amounts. Such amounts can, of course, be rolled over to another plan or used to satisfy the RMD requirement applicable to another of the participant's retirement accounts.

Future guidance should clarify whether a permissible annuity payout under section 1.401(a)(9)-6 can, in any case, exceed the amount that is required under section 401(a)(9). This guidance should provide methods for calculating the RMD applicable to an annuitized contract based on standard calculation rules, but should also provide that annuitized payments that differ from the RMD amount, specifically which exceed the RMD amount, are permissible.

[12] Treas. Reg. section 1.401(a)(9)-6.
[13] See section 402(c)(4)(B).
[14] Treas. Reg. section 1.401(a)(9)-5.

Annuity contracts that have not been annuitized are subject to the RMD rules found in Treas. Reg. section 1.401(a)9)-5.[15] Such contracts are also subject to rules that require "pre-annuitized" RMDs to be adjusted, as necessary, by the actuarial present value ("APV") of any "additional benefits" (such as living or death benefits) that the annuity contract provides. This rule, although somewhat difficult to apply in practice, does not generally impede the use of in-plan lifetime income vehicles. However, the rule does impede the use of annuity contracts characterized "longevity insurance" or "longevity annuities."

A longevity annuity, as this question notes, is a deferred contract that annuitizes at an advanced age. However, unlike a normal deferred annuity, the longevity annuity generally has little to no cash value during the deferral phase. A deferred longevity annuity would become subject to the RMD rules found in section 1.401(a)(9)-5 upon the participant reaching age 70 ½, and generally the RMD calculated for such a contract would be $0.00 because the contract has no cash value. However, the APV rules would apply to such a contract and could produce an actual RMD for a year in which the contract has no cash value. This RMD obligation would likely be funded from other retirement assets, if available. However, the basic purpose of the RMD rules is somewhat lost on an asset that has little to no cash value.

We believe that future guidance should provide that longevity annuities or other in-plan lifetime income options that provide ONLY "additional benefits" as defined in the APV rules should not be subject to RMD requirements. Guidance could provide that if the entire amount of the RMD calculated for the contract is based upon additional benefits, and no RMD amount is required based on the contract's current value, the RMD rules would not apply to any value calculated based on such additional benefits.

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?

Response: Given the wide-variety of guaranteed products offered in the (out-of-plan) individual market, it would generally be unnecessary for investors to roll back to a former employer's plan to gain access to a guaranteed income solution. Additionally, it is unlikely that a participant would consider a former employer's plan for retirement investing, and employers generally would prefer not to resume fiduciary responsibility for former employees.

Portability between out-of-plan assets and a participant's current employer plan should be allowed following current rollover rules.

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[15] Treas. Reg. section 1.401(a)(9)-6, Q&A 12.

<u>*Selection of Annuity Providers*</u>

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

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

Response: Plan sponsors have been slow to adopt the safe harbor standards outlined in 29 CFR 2550.404a–4. The requirement to "engage in an objective, thorough and analytical search for the purpose of identifying and selecting providers from which to purchase annuities" for many plan sponsors feels like a higher bar than the general fiduciary standards that apply to other funds that might be selected by a plan fiduciary. The listing of specific duties and considerations, while helpful in some respects in that it provides an appropriate road map, is viewed by plan sponsors as difficult and causes them to incur additional liability.

Smaller plan sponsors do not have the expertise or resources to hire appropriate experts. (Paragraph (b)(5) of this regulation provides that, if necessary, the fiduciary should consult with an appropriate expert or experts for purposes of complying with the requirements of the safe harbor.) As a result, intermediaries that serve the small plan market do not evaluate and do not recommend adding an annuity option due in part to this regulation.

The Agencies should recognize that group annuity contracts and individual annuity contracts today are widely used as a funding vehicle for defined contribution plans – both 401(k) and 403(b) plans - especially in the smaller end of the market. Most of these annuity contracts will have and will offer as part of the annuity contract various distribution and annuity draw down options. It is not uncommon for these funding vehicles to offer life annuities, life annuities with period certain, joint and survivor annuity payouts, and other annuity payout options. However, the decision by the plan fiduciary to use the group annuity is usually evaluated only on the other features (i.e. the non-annuity payout features) of the contract. For example, the fiduciary and the intermediary will generally evaluate a group annuity contract based on: underlying investments, fees, diversity of investments, brand name, administrative services associated with the contract, record keeping services associated with the contract, ancillary services such as call centers and web site, financial strength of the underwriting organization and other features. As a result, annuity options are offered by many small plans but they are not evaluated under the safe harbor standards of 29 CFR 2550.404a–4 nor are the annuity features widely known or utilized by participants. In fact, we believe that less than 1% of defined contribution plan participants that have access to annuity options take their distribution in the form of an annuity.

Likewise, in the mid-sized and large 401(k) and 403(b) market, clients may use mutual funds as the primary investment vehicle but they often use a guaranteed contract or stable value fund for the fixed income asset class. These contracts, similar to the small end of the

market, will contain a variety of fixed deferred annuity payout options. Like the small market, the annuity payout option associated with the guaranteed or stable value product is not widely known or utilized by participants and not evaluated by a sponsor for its draw down / annuity options.

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?

Response: The DOL should make significant changes to this regulation if the Agencies wish to encourage the use of out-of-plan lifetime income options through the use of guaranteed annuities. If the requirements on the plan sponsor to choose such an insurer are not based on objective criteria, we believe that there will continue to be significant incentive <u>not</u> to provide such a lifetime income option. The problem with the cited regulation is that it imposes a burden that almost all plan sponsors cannot meet without incurring the expense of hiring an outside expert to determine initially and periodically thereafter, for example, "the annuity provider is financially able to make all future payments under the annuity contract…."[16] It would be very helpful if the DOL would provide an objective criteria that a plan sponsor could use for the cited safe harbor and, also, for a needed safe harbor to relate to the choice of an in-plan lifetime income option.

Such objective criteria could relate to an insurer's being licensed within a state and the insurer's standing with that state's insurance department and/or the ratings provided by well known insurance company rating agencies such as A.M. Best and Standard & Poor's. We believe that such objective criteria would provide a more meaningful and up-to-date analysis than could most experts who would have little leverage with an insurance company to obtain important and, perhaps, confidential information necessary to make an evaluation. Such guidance from the Agencies should make clear that the evaluation by the plan sponsor need only be done at the time the insurer is selected and annually thereafter unless the plan sponsor learns in the interim of significant financial problems with such insurer.

The DOL needs to understand that even though the safe harbor regulation being discussed here is clear that it is only a safe harbor and not the sole means of a plan sponsor fulfilling its fiduciary obligation in this context, plan sponsors are understandably unwilling to act outside of the safe harbor. Failing to remedy this matter as described in this response is likely to significantly reduce the availability of lifetime income distribution options from defined contribution plans.

We do not believe that making these changes will compromise important participant protections since we think such objective criteria will provide a better measure of an insurer's financial well being than the more costly, less objective review currently contemplated by this regulation.

[16] See 29 CFR § 2550.404a-4(b)(4).

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?

Response: The safe harbor described in this question should be extended to apply beyond distribution annuities to include annuities that provide for in-plan lifetime income options that accrue benefits over part or all of a plan participant's working career with the plan sponsor.

We believe that the safe harbor should be limited to annuities or other financial products that provide lifetime income benefits guaranteed by the financial solvency of the issuer of such a financial product. We are not aware of any financial product other than an annuity that provides such a guarantee including features attached to annuities such as guaranteed minimum withdrawal or income benefits, i.e., often referred to as GMWB and GMIB, respectively, or more generally as "living benefits."

We note that the Agencies have throughout the RFI inquired about lifetime annuities or "similar lifetime income products." We are not aware of any similar products that provide the guarantee provided by an annuity. We think that any regulations or guidance provided by the Agencies should distinguish between lifetime income products that provide such a guarantee and those that do not. Given the uncertainties of trying to protect against the longevity risk that the RFI recognizes, the response by the Agencies to the RFI responses should recognize that most plan participants will want to protect against such a risk by choosing a lifetime distribution option that provides the guarantee that is uniquely available from an insurance company issued annuity.

ERISA Section 404(c)

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

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

Response: We do not believe that the regulations under ERISA 404(c) need to be amended to facilitate the use of a fixed deferred lifetime annuity option in defined contribution plans. Our experience is that virtually all plans would be able to meet all the fund requirements of 404(c) without the Agencies including additional guidance to enable fixed deferred annuities as a core investment offering. Most plans offer at least a dozen funds where

many of the funds would meet the requirements of a broad range of investments that consists of at least three diversified investment alternatives, each of which has materially different risk and return characteristics. Likewise the diversification requirement and investment transfer frequency requirement can be met by other investment options. Finally, we do not believe there is a correlation of higher use of the investments designated as a core investment. As such, we do not believe it is necessary to include fixed deferred annuities as a core investment as a means to encourage their use. Finally, the information disclosure requirements of 404(c) can and are generally met by including: risk and return characteristics, fees, description of the benefit or income associated with the fixed deferred annuity, restrictions in and out of the investment option, and other investment information.

Our belief is that fixed deferred lifetime annuities or similar lifetime income products offered as part of a 404(c) line up would be offered as non-core investment options.

The advantages and disadvantages of such products are similar to the advantages and disadvantages as outlined in Question #1 above. An additional advantage of a fixed deferred annuity that was purchased incrementally over time would be that the interest rates used to make the purchase would be made over a participant's working lifetime. If the deferred fixed annuity was purchased at retirement during a relatively low interest rate environment, the annuitant would incur additional interest rate and inflation risk. There are other ways to hedge this risk other than purchasing the annuity incrementally over a person's life (for example annuities that invest in TIPS or other investments that correlate to interest rates.) A younger person that purchases a fixed deferred annuity over their working career will also hedge mortality risk that exists if an annuity is purchased at normal retirement age when the participant is older.

If the Agencies prefer to use 404(c) as a way to encourage the adoption of deferred annuities, we would suggest expanding the QDIA regulations and enabling deferred fixed annuities to be part of a valid QDIA and thus get to the 404(c) protections by 2550.404c-5.

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?

Response: We do not believe that the regulations under ERISA 404(c) need to be amended to facilitate the use of lifetime income products through variable annuities in defined contribution plans. Our experience is that virtually all plans would be able to meet all the fund requirements of 404(c) without the Agencies including additional guidance concerning variable annuities or "living benefit" products noted in our response to Question 32 above that have emerged in recent years. Most plans offer at least a dozen funds where many of the funds would meet the requirements of a broad range of investments which consist of at least three diversified investment alternatives, each of which has materially different risk and return characteristics. Likewise the diversification requirement and investment transfer frequency requirement can be met by other investment options. Finally, we do not

believe there is a correlation of higher use of the investments designated as a core investment. As such, we do not believe it is necessary to enable lifetime income / variable annuities as a core investment as a means to encourage their use. Finally, the information disclosure requirements of 404(c) can and are generally met by including: risk and return characteristics, fees, description of the benefit or income associated with the fixed deferred annuity, restrictions in and out of the investment option, and other investment information.

Our belief is that if lifetime income / variable income annuities or similar lifetime income products is offered as part of a 404(c) line up, it would be offered as a non-core investment options.

The advantages and disadvantages of such products are similar to the advantages and disadvantages as outlined in Question #1 above. An additional advantage of a variable annuity / lifetime income is the potential for growth that exists as part of the underlying investments. Also, to the extent the variable annuity enables investments in bonds and equities and offers a floor protection or a guaranteed minimum accumulated benefit (with or without a step up provision), the variable annuity offers peace of mind and protections on a person's accumulated investment.

If the Agencies prefer to use 404(c) as a way to encourage the adoption of variable annuities and lifetime income products, we would suggest expanding the QDIA regulations and enabling variable annuities to be part of a valid QDIA and thus get to the 404(c) protections by 2550.404c-5.

Qualified Default Investment Alternatives

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

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

Response: A number of providers are interested in or have developed in-plan guarantees for employees approaching retirement that provide downside protection against market losses. Downside protection (versus lifetime income) is viewed as a more valuable

guarantee by most participants.[17] Most service providers believe that life cycle funds and life cycle managed accounts will continue to be the most widely adopted QDIA. A number of providers have integrated in-plan guarantees with life cycle funds and have offered such vehicles as viable QDIAs. One provider has even provided warranty language that provided some legal protection to plan sponsors if the QDIA was found to be an invalid QDIA due to the associated guarantee.

Plan sponsors and intermediaries have been slow to adopt these guarantees as part of the QDIA and automatically defaulting participants into the guarantee product. Because the QDIA regulations specifically delineate the investments that could be offered as a QDIA and since the regulations did not mention or consider associated guarantees that can be included in the QDIA, most plan sponsors are hesitant to add such features to their QDIA. If the DOL stated through formal guidance that the addition of a guarantee to an otherwise valid QDIA would not in and of itself cause the investment option to no longer enjoy QDIA status, adoption of such in-plan guarantees would see a measurable increase. Providing fiduciaries cover and guidance will make plan sponsors more confident that they can offer such products as part of the QDIA and / or automatically add such a guarantee to an account at a certain age through a negative election process.

We do think it advisable for the Agencies to take action to permit the use of lifetime income features as QDIAs. While we believe that the Agencies should encourage the availability of lifetime income distribution options in defined contributions plans, we believe that the selection of such a distribution benefit is so personal to the plan participant that its use as a QDIA requires greater caution on the part of the plan sponsor since the QDIA is intentionally designed to provide more standard investment options of which the plan participant can take control at any time. Some lifetime income distribution options are not so flexible as to permit a plan participant defaulted into it to easily make changes. With that understanding, we still believe that in-plan lifetime income options in defined contribution plans will provide needed financial security to many plan participants and that a plan sponsor should be able to include such an option in its plan's QDIA and get the protection currently provided to plan sponsors who choose a QDIA in compliance with the applicable rules.

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

Executive Order 12866 (EO 12866) requires an assessment of the anticipated costs and benefits of a significant rulemaking action and the alternatives considered, using the guidance provided by the Office of Management and Budget. In addition, the Regulatory Flexibility Act (RFA) may require the preparation of an analysis of the economic impact on small entities of proposed rules and regulatory alternatives. For this purpose, the Agencies consider a small entity to be an employee benefit plan with fewer than 100 participants. The Paperwork Reduction Act (PRA) requires an estimate of how many "respondents" will be required to comply with any "collection

[17] Teleconference and Life Web meeting sponsored by LIMRA on participants and retirement income products April 2010.

of information" requirements contained in regulations and how much time and cost will be incurred as a result.

The Agencies in this section of the RFI are requesting comments that may contribute to any analyses that may eventually need to be performed under EO 12866, RFA, and PRA, both generally and with respect to specific areas identified in questions 36 through 39.

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

Response: There will be costs associated with adding lifetime income options to the employer retirement plan market, and some of these costs will likely be passed on to plan sponsors and then participants. Initially, some service providers will need to enhance their platforms to record-keep and administer guaranteed investment options such as annuities. Ongoing there will be additional expense to service plans and participants with lifetime income options given the potential complex nature and lack of investor knowledge concerning lifetime income products. These costs could be lowered with the creation of industry standards for product designs and data layouts.

Plan sponsors who offer lifetime income products will have the benefit of being able to ensure that participants (and employee prospects) have access to an investment option within the plan that allows for guaranteed income for life. Additionally, to the extent that in-plan annuity options will drive persistency of assets remaining in the plan after termination, sponsors may benefit from lower record-keeping fees due to larger plan size.

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?

Response: Similar to existing pricing practices in the defined contribution plan industry, the costs that are outlined in Question 36 are more likely to be passed on to smaller plan sponsors than large plan sponsors.

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?

Response: Making a lifetime income option a default distribution election alone likely will not impact participant contribution rates. Adding estimated lifetime income payout information to participant statements and other communications could help increase contributions by enhancing participant knowledge of how plan balances covert to income streams in retirement.

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?

Response: For plans that offer annuity payout options, less than 1% of participants elect to annuitize all of their assets. On the individual (out-of-plan) side, approximately half of investors who purchase an annuity elect a living benefit rider or annuitize into an income stream.

Summary

We believe that the Agencies focusing their efforts on out-of-plan or in-plan options selected at the time of termination of employment or in the later stages of an employee's working career, including, importantly, education of plan sponsors and participants about such distribution options, will go a long way toward providing the lifetime income options that plan sponsors and plan participants will actually use. While we strongly support the use of defined contribution plan assets to provide lifetime income options to plan participants, we are not convinced that the use of limited resources available to plan sponsors and their investment product and service providers necessary to provide for in-plan distribution options that accrue over decades of employment will be successful in, or necessary to, providing lifetime income protection to plan participants. As noted in our responses, our experience is that plan participants begin planning for retirement and aggregating assets later in their working careers. Providing education and incentive to select a lifetime income distribution option at that time will, we believe, provide for the most efficient use of resources and the greatest likelihood of success. There are more than enough lifetime income options available as out-of-plan or in-plan options selected at the time described in this paragraph that an employer can make available to its plan participants if the rules issued by the Agencies encourage it.

Finally, we believe that it is important for the Agencies to address the required use of unisex criteria in determining the amount of in-plan lifetime income options to encourage their widespread use since men will be able to get significantly higher benefits out-of-plan. Providing ways for employees to be successful in planning for retirement will only work if an employee believes that the benefit provided is a fair exchange for cost paid and that will only happen if the lifetime income option can be readily understood and compared to other distribution options.

If you would like additional information, we would be happy to discuss any request that you have. Please contact the undersigned with any questions or requests.

Very truly yours,

David J. Kolhoff, Senior Counsel