Lincoln Financial Group®

Statement of

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Employee Benefits Security Administration
Joint Hearing
with the
U. S. Department of Treasury
on
Lifetime Income Options For Retirement Plans

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Members of the joint panel … my name is Eric Levy … and I am Vice President and Head of Defined Contribution Products for Lincoln Financial Group. Lincoln Financial has participated in the retirement plan marketplace for more than fifty years … and today serves more than 24,000 plan sponsors and their 1.4 million plan participants in the corporate, healthcare, education and non-profit sectors. We are a leader in developing lifetime income solutions for both individual products and defined contribution plans, including a product called i4Life® Advantage that was the subject of a Private Letter Ruling issued in September 2009. I appreciate the opportunity to appear before you today to share our views about the importance of ensuring that plan sponsors have the guidance they need to offer appropriate income options to help their employees face their futures with confidence.

Plan participants face a number of risks when they begin to take distributions from their defined contribution retirement plans … including longevity risk – the risk that they may outlive their stream of income … and inflation risk – the risk that the income stream may lose purchasing power over an extended period of time. Only insurance companies have the ability to assume the risks of individuals … and are able to offer the product solutions – specifically annuities – to provide guaranteed benefits. Lifetime annuity payments from an insurance company can be an excellent solution for providing an income stream that plan participants cannot outlive … while variable annuities or fixed annuities with inflation adjusted payments can be chosen to combat inflation risk.

Insurance company annuities have some perceived disadvantages. They are sometimes viewed to be irrevocable, inflexible and inaccessible … and costly relative to other options. A new generation of annuity product designs, however, addresses these perceived disadvantages. One such design is Lincoln Financial's i4LIFE® Advantage rider, which is administered through a patented method that provides a lifetime income stream with substantial flexibility and complete accessibility during an access period of the participant's choosing. Newer product designs also include reasonable and simplified fee structures, and costs can be lowered appreciably when purchasing the annuity inside a defined contribution plan.

We believe that clearer guidance on incorporating lifetime income products in defined contribution plans would significantly benefit plan sponsors and plan participants. Such guidance could also help to ensure that these products are prudent and sound from a fiduciary perspective. And if employers were simultaneously encouraged to provide more education about available choices, costs and features … and to provide clear illustrations showing how much income participant account balances will convert to in order to fund their retirements … more plan participants would understand the very real threats to their long-term financial security posed by longevity and inflation … combined with impact of the decisions they are making today regarding their contribution rates, asset allocation and, in too many cases, unfortunately, hardship withdrawals and/or loans. Further, participants would understand that there are solutions and resources available to help them plan to minimize these threats.

Turning to fiduciary obligations … in our opinion, only annuities – with their lifetime income options and guarantees backed by the full faith and credit of the issuing company – should be the subject of the safe harbor. Any lifetime income option that does not provide such guarantees should be subject to standard fiduciary determinations. The size of the plan should not come into play in these guidelines, since the fiduciary obligation owed the participants by the plan sponsor is the same no matter the size of the plan. And the criteria required in the selection of a provider should be objective and easily determined.

While current safe harbor regulation is an improvement over "safest available annuity" rules, it is still not practical. The requirement to evaluate an insurer's future solvency means that all but a very narrow segment of plan sponsors must hire an outside expert to make that determination, since it requires a detailed review of an insurer's financial records, investments, and current and future obligations. In addition, it is unclear how such an independent expert would obtain access to this information, making the requirement not only difficult, but impossible, to meet.

Information on the financial strength of insurance companies is readily available from state insurance regulators and from private industry rating agencies which routinely have access to the detailed information needed to make a reasonable determination about future claims paying ability. State insurance regulators can be encouraged to coordinate access to basic insurer financial information, licensing and standing with state departments of insurance.

Safe harbor rules can and should be expanded to cover the selection of an annuity provider for an "in-plan option" as described in the Request for Information … and should not be limited to a selection for benefit distributions from defined contribution plans as is currently the case. However, since many plans are already funded with group and individual annuities that incidentally provide for distribution in the form of an annuity, the safe harbor should not be modified to inadvertently include the selection of the annuity to fund the plan as an act contemplated by the safe harbor … and therefore subject to a fiduciary standard beyond the normal fiduciary requirements where a plan sponsor selects its plan funding vehicle whether that funding vehicle is a mutual fund, a bank financial product or an annuity contract.

Ultimately, there is no single, simple solution to address the multiple concerns about best options for including lifetime income in retirement plans. We believe that it will take a joint effort between insurance providers – who have the regulatory structure and risk management expertise to offer guarantees … asset managers – who are skilled at developing products to maximize savings and accumulation … and recordkeepers – who provide the systems, statements, web experiences, call centers and in-person service. Such partnerships could result in pricing efficiencies, clearer delivery, and diversification of other risks from the plan sponsor's viewpoint. These partnerships – along with new concepts of plan design – are being widely explored today.

Turning to plan design … how retirement income products are integrated into a retirement plan – and how plan sponsors and service providers describe and communicate the benefits of these options – can have an effect on their usage by plan participants. One seldom-discussed but significant barrier to more widespread adoption and use is the requirement for unisex rates for in-plan lifetime annuities. Advisors generally educate plan sponsors and plan participants to the fact that males can receive higher lifetime benefits through gender-distinct rates in an Individual Retirement Annuity than through an in-plan unisex lifetime annuity. In-plan unisex lifetime annuity payouts in a defined contribution plan are usually based on 100% female or a 50%/50% blended rate due to the expectation that most or all males will roll out of the plan to receive a higher gender-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. By comparison … for life only, annual income for males is 7.3% higher than for unisex options. Plan fiduciaries are reluctant to encourage their male retirees to access in-plan annuities if they know that they would be better off with an out-of-plan retirement income annuity option. 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.

There is positive news of how plan design innovation has led to more favorable participation in retirement plans. Behavioral Economics studies earlier this decade showed that a typical 401(k) or 403(b) plan with automatic enrollment features dramatically increased participant rates – from 67% to near 90%. Further, automatic step-ups and automatic investing in a QDIA proved to increase retirement security for many plan participants, and especially rank and file employees. This same concept could be leveraged to encourage the appropriate use of retirement income products and downside protections for participants. Specifically, guidance that explicitly states the prudence of automatically providing downside protections and retirement income products into already chosen or defaulted investments – such as target date funds – as participants enter a period 10 to 15 years prior to retirement date … would provide plan sponsors the comfort they seek in offering such products and ultimately improve outcomes.

As more and more individuals rely on savings built up in employer-sponsored defined contribution plans for financial security in retirement, the more critical it becomes that plan sponsors have clear and simple guidance in terms of fiduciary responsibility and the incorporation of income options to improve outcomes for plan participants. Thank you for your time and attention on this important topic.