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Definition of an Investment Advice Fiduciary

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Retirement Security Rule: Definition of an Investment Advice Fiduciary

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Submitter Information

Name: James Watkins

General Comment

The proposed Retirement Security Rule addresses a much needed method of supervising and overseeing the reccomendations of otherwise unregulated fixed indexed annuities (FIAs). While FIA advocates will point to the NAIC's suggested guidelines, such guidelines are non-binding on states and, as the DOL's release points out, are essentially aspirational, as the NAIC has no authority to enforce such guidelines.

While approximately 40 states have adopted the NAIC's guidelines in one form or another, the fact that there is currently no federal oversight and enforcemement of such guidelines has resulted in inconsistent and inequitable protectiion of employees and retirees in connection with rollovers from 401{k} and 403(b) plans into various types of annuities. While the annuity industry chants its "guaranteed income for life" mantra, they do not provide that an annuity owner will receive a commensurate return from an investment in an annuity. Since rollovers are not covered under ERISA, annuity issuersare not required to provide rollover customers with the "sufficient information to make an informed decision" required under ERISA Section 404(c), information such as breakeven analyses and the potential impact of spreads, caps, and participation rates. Such information often exposes the fact that while the annuity owner may receive some income for life, the terms of the annuity, and the fact that issuer often reserves the right to unilaterally change such terms annually, often reduces the odds that the annuity owner will even break even. In many cases, this essentially guarantees that the FIA issuer will receive a windfall, which the FIA issuer can then use to subsidize its legal obligations to other annuity owners. The lack of providing a commensurate return to the annuity owner, combined with the annuity issuer's control over the annuity contract's terms and the right to unilaterally chages such terms to ensure a windfall, are the antithesis of a fiduciary's duties of prudence and loyalty. While ERISA's stated purpose is to protect employees by promoting equitable situations to allow them to build up resources for retirement, the current unregulated situation with FIAs allows the annuity industry to effectively negate ERISA's protections and effectively allows the FIA issuer to place its best interests ahead of the annuity owner's best interests.

A Wall Street Journal article, entitled "Big insurers avoid equity-indexed annuities," noted that MassMutual conducted a study of the performance of the performance of indexed annuities relative to the S&P 500, both with and without dividends included, The study covered the 30-year period ending Deember 2003.

The study concluded that the indexed annuity, which used the S&P 500 as its benchmark, underperformed in both S&P scenarios (31.76% without dividends, 52.45% with dividends). The article noted that the indexed annuity even underperformed Treasury bills over the same period.

Dr. William Reichenstein of Baylor University wrote an article entitled "Can Annuities Offer Competitrive Returns?" Dr. Reichenstein concluded that the design and the costs associated with indexed annuities effectively prevents them from providing competitive returns when compared to other available investment options, His findings were consistent with the earlier findings of Nobel laureate Dr. William F. Sharp and other investment icons - costs matter. As John Bogle said, "you get what you don't pay for."

While the annuity industry likes to engage in misleading games of semantics, such as "no fees" versus "costs," the ultimate impact of costs and artificial restrictions, such as caps and participation rates, on reducing an annuity owner's realized return is undeniable.