Draft Testimony of
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Distinguished members of the ERISA Advisory Council, thank you for inviting me to speak with you today.

My name is Mark Foley, and I am a Managing Director and Head of Default Solutions at TIAA. I am grateful for this opportunity to share TIAA's views on how policymakers can improve retirement security for all Americans. Specifically, I look forward to discussing how to best address the challenges Americans face when it comes to making their savings last throughout their retirement years.

TIAA is the leading provider of retirement services for those in the academic, research, medical, and cultural fields. For one hundred years, TIAA's mission has been to aid and strengthen the institutions and participants we serve by providing retirement and financial solutions that meet their evolving needs. Today, TIAA manages more than $1 trillion in assets for the 5 million participants we serve across more than 15,000 institutions. With our strong not-for-profit heritage, the mission we embarked on in 1918 is more relevant today than ever as we remain dedicated to serving the financial needs of those who serve the greater good.

One key characteristic of TIAA's retirement plans is the ability for retirement plan participants to allocate a portion of their retirement savings to annuity products that guarantee a certain level of return while they save for retirement. At retirement, they have the option, but not the obligation, to seamlessly convert some or all of that balance to a guaranteed income stream that they can never outlive. Due in part to the risk-pooling concept at the center of insurance products like annuities, employees who annuitize assets benefit from competitive guaranteed payment amounts. This contributes to highly successful outcomes for our participants, who are able to retire with the comfort of knowing that they will have a stream of income that they, and if so elected, their beneficiaries cannot outlive. As we celebrate our 100th anniversary, we are proud of the fact that over the years we have paid out more than $400 billion in retirement benefits. In 2017 alone, TIAA paid out over $5 billion to our retirees, including 32,000 recipients over the age of 90, each of whom receives monthly annuity payments.

Ensuring that Americans can save sufficient assets for retirement *and* be able to convert those assets into an income that is guaranteed to last throughout their retirement is among the most critical issues facing our economy over the next generation. With 10,000 baby boomers retiring each day, the total number of U.S. retirees will rise to over 66 million by 2025 and over 80 million by 2040.[1] Today, Americans can anticipate 20 to 30 years or more in retirement. In fact, more than half of 65-year-old men will live beyond age 85 and one in three is expected to live to at least age 90. Life expectancy is even higher for women; nearly two-thirds of 65-year-old

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[1] Social Security Administration, *Annual Performance Plan for Fiscal Year 2012*, 2011, at 36, available at: https://www.ssa.gov/agency/performance/materials/2012/APP%202012%20508%20PDF.pdf

women are expected to live to age 85 and almost half will live to age 90.[2] Longer life expectancy is a remarkable societal achievement, but it also increases "longevity risk," that is, the chance that retirees will outlive their savings. It also means that those people that are living longer may also be living with some level of cognitive decline making it more difficult to manage their own decumulation strategy in some cases.

Central to addressing this challenge is adopting policies that will increase access to annuities – the only products available that can truly guarantee a stream of income that will last throughout retirement. In fact, there is a consensus among economists that annuities offer exceptional protection from retirees longevity risk, as well as the other risks mentioned. Unfortunately, annuity products are largely missing from the retirement plan investment menus of U.S. private corporations, resulting in a significant segment of retirement savers not having in-plan access to such products.

Providing access to annuities inside retirement savings plans offers meaningful benefits to participants. In-plan annuities can offer competitive pricing since institutionally-priced products leverage economies of scale. The oversight and due diligence that an employer exercises over their plan helps ensure that participants have access to competitive and beneficial offerings. Giving plan participants direct access to annuitization vehicles can reduce the risk of leakage through lump sum distributions. And, perhaps most importantly, in our experience those who save using in-plan annuities have a higher rate of annuitization at retirement.

Despite these and other benefits, a recent study revealed that only 5 percent of 401(k) plans offer participants access to an in-plan annuity product.[3] By contrast, 84 percent of employer-sponsored 403(b) plans, TIAA's core market, offered fixed annuities as an investment option.[4] As a result, when many 401(k) plan participants retire, they often do not have direct access to the products that can make their savings last for the rest of their lives. Instead, they often need to educate themselves and shop for annuity products in the retail market. While retail products have and continue to play an important role in retirement security, we believe that having these products also available through an employer-sponsored plan is key to addressing concerns about retirement income.

The fact that 403(b) participants have more access to lifetime income options in their retirement plans stems from the different histories of 401(k) and 403(b) plans. The 401(k) plan was initially intended to provide supplemental retirement savings for employees of private corporations who typically had defined benefit lifetime pension income, in addition to Social Security income, that they could use to help them meet recurring living expenses in retirement. However, for reasons outside the scope of this testimony, in the last 25 years the 401(k) supplemental savings plan has

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[2] These data are based on calculations for non-smoking individuals with average health using the Actuaries Longevity Illustrator developed by the American Academy of Actuaries and the Society of Actuaries, available at: http://www.longevityillustrator.org/

[3] *401(k) Plans Cautious About Adding Guaranteed Income Products*, Plan Sponsor, Jan. 2017, available at: http://plansponsor. com/401k-Plans-Cautious-About-Adding-Guaranteed-Income-Products/

[4] Brightscope, *The Brightscope/ICI Defined Contribution Plan Profile: A Close Look at ERISA 403(b) Plans* (2015), at 21-24, available at: https://www.ici.org/pdf/ppr_15_dcplan_profile_403b.pdf

become the predominant workplace retirement plan for corporate employers.[5] Thus, the risk of generating sufficient income in retirement has largely shifted from the employer to the employee.

The 403(b) plan, in contrast, actually predates the 401(k) and was designed to provide lifetime retirement income to educators and others employed by not-for-profit entities. It still retains many of its original features and over time has evolved into what can best be described as a hybrid retirement savings plan, providing participants with the opportunity to both save in and then receive income from the same plan. While 401(k)s can be an excellent way to accumulate funds for retirement, we believe they could be significantly improved with a few regulatory changes that would remove roadblocks and encourage 401(k) sponsors to adopt in-plan annuity vehicles.

The foundation of a successful retirement is ensuring an individual has a base of steady, predictable guaranteed income that will last throughout his or her retirement years. Access to annuity products also minimizes the risk of poverty among retirees and reduces the strain on the social safety net provided by the Federal government. Having more in-plan annuity options available to workers directly through employer-sponsored retirement plans is core to the very purpose of the retirement savings system—to ensure individuals can attain a financially secure and independent retirement.

Drawing on our experience as the nation's leading provider of in-plan lifetime income solutions, TIAA developed a white paper entitled, *Closing the Guarantee Gap,* that includes six central recommendations that policymakers should pursue in order to encourage the adoption of annuity products on retirement plan menus. Those recommendations include:

1. Simplify the safe harbor for employers selecting an annuity provider.
2. Increase the portability of annuity contracts.
3. Broaden the qualified default investment alternative (QDIA) regulations so that annuities can become default investments.
4. Provide retirement savings plan participants with an annual lifetime income disclosure statement.
5. Give participants more access to flexible income distribution options.
6. Provide favorable tax treatment for annuity income in retirement.

By changing federal policy in several key areas, these solutions will help to advance the role of lifetime income in retirement savings plans. For the purpose of this testimony, I'd like to focus on two of these recommendations: simplifying the annuity selection safe harbor and broadening the QDIA regulations.

Simplifying the Annuity Provider Selection Safe Harbor
TIAA strongly supports amending the DOL's existing regulatory safe harbor for selecting an annuity provider for individual account plans (the "safe harbor"). We note that the ERISA Advisory Council recommended revisiting the annuity provider selection safe harbor in 2012.

[5] Investment Company Institute, *2017 Investment Company Factbook: A Review of Trends and Activities in the U.S. Investment Company Industry*, 2017.

One of the primary reasons employers have been reluctant to offer annuities on their plan investment menus is uncertainty about how to adequately satisfy their legal responsibilities when selecting an annuity provider.[6] The DOL has taken steps to provide employers and their legal counsel with a safe harbor that would guide this decision and encourage the inclusion of annuity products in retirement plans. Unfortunately, this existing safe harbor has gone largely unused as plan sponsors have signaled the need for more certainty in the safe harbor's terms.

A key uncertainty has been the appropriate process that fiduciaries should follow when evaluating the financial strength of an insurance company that would provide an annuity. Evaluating the financial strength of any given annuity provider can be a complex process. While the intention of the existing safe harbor is to simplify this process, it lacks the clear guidelines that many plan fiduciaries desire and for that reason, many plan fiduciaries are reluctant to adopt in-plan annuities, even if they and their plan consultants recognize the value annuity products can deliver to their particular employee population.

DOL can address this by establishing clear and objective guidelines that would help plan fiduciaries choose an annuity provider for their plan with the confidence that they have met the guidelines. DOL can address these concerns by establishing clear and objective guidelines that plan fiduciaries can follow when choosing an annuity provider. TIAA believes the rules should allow employers to rely on representations that an insurer is licensed to offer guaranteed retirement income contracts and has met certain regulatory requirements under state insurance regulations. In essence, the safe harbor should allow fiduciaries to rely on the true experts in evaluating an insurer's financial strength – the state regulatory bodies. Bipartisan legislation was recently introduced in Congress that lays out the specific framework for this safe harbor.[7]

We strongly believe these changes would clear a significant hurdle to the availability of annuity products on employer-provided retirement plan menus. While the decision to adopt in-plan annuity products would still remain with the employer, simplifying the annuity provider selection safe harbor will help ensure that more American retirees will have an institutionally-priced in-plan annuity option that will allow them to use some of their retirement savings for its intended purpose – providing a steady stream of retirement income they will not outlive.

Lifetime Income as Default Investments

Another step that DOL could take to encourage the inclusion of annuities in retirement plans is to amend the Qualified Default Investment Alternative ("QDIA") regulation. The QDIA rules provide a safe harbor for plan sponsors when determining an appropriate investment vehicle into which they can default their employees' retirement plan contributions. Of the potential investment options that qualify under the QDIA safe harbor, the most utilized has been and continues to be target-date funds. In fact, over 75% of defined contribution plan sponsors electing to use the QDIA safe harbor default their participants into target-date funds.[8]

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[6] Government Accountability Office, *401(k) Plans: DOL Could Take Steps to Improve Retirement Income Options for Plan Participants*, Aug. 2016, at 17, available at: http://www.gao.gov/products/GAO-16-433

[7] The Increasing Access to a Secure Retirement Act (HR 4604), introduced by Congressman Tim Walberg (R-MI) and Lisa Blunt Rochester (D-DE),

[8] *Choosing default investment alternatives for 401(k)s requires due diligence*, Investment News, May 25, 2016.

While we believe the current QDIA safe harbor represents excellent progress in ensuring retirement plan participants are defaulted into diversified and well-managed portfolios like target date funds, the overwhelming majority of these default products have one significant shortcoming – the absence of guaranteed annuities within the investment. To address this shortcoming, TIAA has developed a solution that incorporates a guaranteed fixed annuity into a target date framework. This one simple change can better mitigate the real risks participants face in retirement planning – including market risk, inflation risk, interest rate risk and longevity risk – and actually delivers the guaranteed income most investors think comes from a target date fund. However, due to language in the current QDIA safe harbor that requires any assets invested in a QDIA product be fully liquid at least once every 90 days, it has been challenging for our plan sponsors to get the maximum value this innovative product can offer as a default option for their participants.

The policy behind the QDIA safe harbor is to encourage *long-term* investments appropriate for assets being saved for retirement that can help generate a secure retirement. To that end, DOL made clear in its final regulation that annuities are permissible under the safe harbor.[9] Further, Congress made clear in the legislation directing DOL to promulgate the QDIA regulations that the key to an appropriate default investment is that it include "a mix of asset classes consistent with capital preservation or long-term capital appreciation, or a blend of both." [10] But the QDIA's 90-day liquidity requirement eliminates the possibility of using many kinds of annuity products that provide the types of guaranteed returns and income referenced earlier. This is because in many cases the actuarial considerations that have to be taken into account to offer these guarantees effectively prevent these guaranteed products from meeting a 90-day liquidity requirement. Simply put, providing high-value, long-term guarantees requires the underlying investments to be long-term, and therefore less liquid in nature.

Despite the 90-day liquidity requirements, we believe that guaranteed illiquid annuities are entirely appropriate investments and should be incorporated into the mix of asset classes that make up QDIAs. Given the long term time horizon of retirement investors, a higher yielding yet less liquid fixed annuity can be more effective in delivering better outcomes during the savings years and throughout retirement. In addition, there is evidence that retirement savers want guaranteed income products in their retirement asset mix. In a recent survey of Americans over 40, 76% said income certainty is more important than the performance of their investment portfolio.[11] Surveys also have shown that many retirement savers believe target-date funds already provide guaranteed income in retirement,[12] when the fact is that the overwhelming majority of target-date funds do not include this feature.

Unfortunately, as mentioned earlier, the QDIA's liquidity requirements make it difficult – if not impossible – for plan sponsors to get the greatest value out of the innovative solutions TIAA has

[9] See 29 CFR 2550.404c-5 (e)(4)(vi)
[10] The Pension Protection Act of 2006, P.L. 109-280, § 624(a), Aug. 17, 2006.
[11] Texas Tech Retirement Income Flexibility Study (December 2015) (survey over 1,000 Americans age 40 and older).
[12] Siegel and Gale, *Investor Testing of Target Date Retirement Fund (TDF) Comprehension and Communications*, Submitted to the Securities and Exchange Committee, February 15, 2012 ("Only 36% of respondents correctly indicated that a TDF does not provide guaranteed income in retirement; for TDF owners, the correct response rate was 48% and for non-TDF owners, the correct response rate was 26%").

developed because some of our most efficient guaranteed lifetime income products do not meet the liquidity requirements.

Fortunately, however, we have found the DOL very open and receptive to working toward solutions that would pave the way for higher yielding yet lower liquidity annuity products to be included in QDIAs. In fact, we worked closely with DOL on this issue and applaud them for the Information Letter they provided to TIAA in 2016.[13] The letter confirms that plan sponsors can prudently default participants into investment products with delayed liquidity lifetime income features. We believe the letter helps debunk the marketplace myth that the only plausible default is a QDIA. In other words, the safe harbor is not the water's edge. The letter also implies that a sensible, integrated approach to retirement planning should combine annuities with target date strategies and other investment vehicles to achieve lifetime income that participants cannot outlive.

We are encouraged by the Information Letter and the interest the Advisory Council has taken in this issue. We are hopeful that there is adequate momentum for the DOL to move forward with pursuing changes to the current QDIA safe harbor that will provide some form of relief from the 90-day liquidity rule and remove barriers to ensuring retirement savers have access to guaranteed lifetime income solutions.

Additional Approaches to Increasing Access to Lifetime Income

In addition to the recommendations discussed above, we believe that DOL should consider other policy changes to increase workers access to and utilization of lifetime income options in their workplace retirement plans.

Lifetime Income Disclosure

An important body of research indicates that, if given information about annuities as if they were similar to an investment fund, people tend to prefer the investment fund. Yet, if instead people were given information describing the annuity's ability to produce a stream of income, many more prefer the annuity.[14] Under current law, however, plans are not required to give participants basic information about how to translate their savings into a stream of income.

To enable plan participants to better understand the benefits of lifetime income options such as annuities in a retirement portfolio, we advocate including lifetime income projections in an annual account statement. The statement would provide participants with an annual "checkup" on how their current investments would translate into income in retirement and increase financial literacy about the importance of viewing one's retirement account holistically as a means of accumulating assets for the primary reason of receiving retirement income from those assets.

Annuity Portability

Under ERISA, plan fiduciaries must monitor the appropriateness of the investment menu available to participants in their workplace retirement plans. As part of their review process, fiduciaries sometimes decide to change investment options offered to participants—or switch

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[13] https://www.dol.gov/agencies/ebsa/employers-and-advisers/guidance/information-letters/12-22-2016.

[14] Jeffrey R. Brown et al., *Framing and Annuities*, TIAA-CREF Institute, Trends and Issues, Jan. 2009, available at: https://www.tiaainstitute.org/sites/default/files/presentations/2017-02/report_ti_framingannuities_0109.pdf

entirely from one investment firm to another. But if a fiduciary decides to eliminate an annuity option from the investment menu, the current regulatory framework does not provide clear standards for transferring accumulated income balances in a manner that lets plan participants preserve the annuity's guarantee features.

A plan sponsor's decision to remove an annuity product from the menu of investment options should be treated as a "distributable event." That would make any participant invested in the product eligible to convert the annuity contract to an individual certificate or "roll over" the entire amount invested in the contract to an IRA that includes the insurer's equivalent (or near-equivalent) lifetime-income product. By treating a plan's discontinuation of an in-plan annuity product as a distributable event, participants would maintain significantly similar rights and benefits under their existing annuity contracts—while also preserving tax benefits available through a workplace plan. Additionally, such an enhancement to portability would ease administrative burdens on fiduciaries and reduce employers' reluctance to include annuity options in their investment menus.

E-Delivery

Encouraging the use of electronic delivery ("e-delivery") of retirement plan documents is another area where DOL can make changes that would improve retirement security by reducing the cost of retirement savings plans and increasing savers' access to critical information. Even as Americans increasingly rely on electronic media for financial matters, today's regulatory framework relies heavily on paper delivery of financial documents. Moreover, considerable confusion results from the fact that multiple legal and regulatory standards govern the methods by which financial documents can be delivered. TIAA supports efforts that would make it easier for employers to default employees into e-delivery of relevant financial documents while also keeping important consumer protections in place.

Conclusion

Thank you for the opportunity to testify and for your commitment to improving and modernizing America's retirement system. I'm confident that with the help of interested parties like yourselves and all who are here today, combined with smart policy solutions, we can improve retirement security for all Americans. I look forward to your questions.