



714 Hopmeadow Street • Suite 3  
Simsbury, Connecticut 06070  
860 • 658 • 5058

July 5, 2005

Office of Participant Assistance  
Employee Benefits Security Administration  
US Department of Labor, Room N-5623  
200 Constitution Ave., NW  
Washington, DC 20210

**Re: 2006 National Summit on Retirement Savings**

Dear Sir or Madam:

The NDCC/SPARK Institute, Inc. (“SPARK”)<sup>1</sup> appreciates the opportunity to respond to the Department’s request for comments concerning the 2006 National Summit on Retirement Savings (“2006 Summit”). SPARK believes that the following topics are of critical importance and should be addressed at the 2006 Summit:

1. Automatic Retirement Savings
2. Retirement Income Planning
3. Retirement Plans for Small Businesses

SPARK represents the interests of a broad based cross section of retirement plan service providers, including banks, mutual fund companies, insurance companies, third party administrators and benefits consultants. SPARK members include most of the largest service providers in the retirement plan industry and the combined membership services more than 95 percent of all defined contribution plan participants. SPARK members have significant experience with employee behavior in retirement plans because of our role in the industry. Our members are the plan service providers that are largely responsible for delivering participant education to a substantial majority of retirement plans.

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<sup>1</sup> In March 2005, The SPARK Institute, Inc. and the National Defined Contribution Council completed a merger of the two organizations. The combined organization established a single voice for retirement plan services providers in Washington, D.C.

## **I. Automatic Retirement Savings - “Educate Me” or “Do it For Me”**

SPARK members have significant experience with and have spent millions of dollars on employee retirement education programs, tools and strategies. Our members create the plan enrollment materials, create the retirement and investment education materials, conduct the employee meetings, hear what employees are asking for and understand what they need. It’s clear that the current models to encourage plan participation and savings, and better plan investment decisions have failed despite the years of efforts and millions of dollars spent by employers and service providers to overcome employee inertia and the propensity to do nothing.

According to data from RG Wuefling & Associates,<sup>2</sup> this has resulted in too many employees that still do not participate, do not save enough, and invest poorly even when they do participate. Specifically, the RG Wuefling data showed that participation rates for eligible employees have remained essentially unchanged over the past four years at 75%. In addition, deferral rates have remained steady at six percent, regardless of any company matching contributions. Interestingly, as the RG Wuefling data indicates, deferral rates remain stagnant even though participants indicate that they intend to increase their deferral rates in the coming year. The net result of this low savings rate is that the average participant account balance at the end of 2004 was about \$40,000. Even more alarming is that the median account balance (which is probably more representative of the typical participant) is less than \$15,000.

Although some participants are willing to take an active role in saving and investing for retirement, a significant percentage of employees do nothing or start too late because of the power of inertia. SPARK believes that in order to better encourage individuals to save for retirement and help them make better investment decisions, legislative and regulatory policy should harness the power of inertia that currently acts as a force that impedes retirement savings. Many studies about individual behaviors regarding saving for retirement show that by leveraging inertia employers can help passive employees save and invest for retirement. One such study shows that participation rates by employees hired after the adoption of autopilot features were 30% higher than the employee population hired before such a feature was adopted.<sup>3</sup> In addition, another

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<sup>2</sup> Robert G. Wuefling, *Marketplace Outlook*, 2005 Marketplace Update.

<sup>3</sup> James J. Choi, David Laibson, and Brigitte C. Madrian, “*Plan Design and 401(k) Savings*” *National Tax Journal*, vol. 52(2) (June 2004). See also Brigitte C. Madrian and Dennis F. Shea, “*The Power of Suggestion: Inertia in 401(k) Participation and Savings Behavior*”, *The Quarterly Journal of Economics* (November 2001); Richard H. Thaler and Shlomo Benartzi, “*Save More Tomorrow™: Using Behavioral Economics to Increase Employee Saving*,” *Journal of Political Economy*, vol. 112(1) (February 2004); and Patrick Purcell, “*Automatic Enrollment in Section 401(k) Plans - Congressional Research Service*” The Library of Congress (October 14, 2004). Many other studies by James Choi, David Laibson, Brigitte Madrian, Richard Thaler, Shlomo Benartzi and others support the notion that inertia and passive behavior can be leveraged to increase retirement savings.

recent study shows that during plan reenrollment approximately 90% of employees enrolled through an automatic enrollment feature either kept their deferral percentage the same or increased it.<sup>4</sup> Additionally, a Hewitt Associates study showed that in an automatic enrollment plan nearly 40 percent of participants with two years of participation remain in the conservative default investment option.<sup>5</sup>

SPARK believes that the focus of legislative and regulatory policy and programs should promote automatic retirement savings programs to help employees who need help the most have someone “do it for me.” Automatic retirement savings programs include any defined contribution plan such as a 401(k) plan in which the employer adopts plan design features such as automatic enrollment, automatic deferral increases, and managed or automatic investing that are intended to help long term employees to save and invest for retirement. Information, tools, materials and resources for employees who are already or are willing to be actively engaged in their retirement planning exist in abundance. Automatic retirement savings plans would not prevent actively engaged individuals from controlling their preferred retirement savings approach.

Although automatic enrollment is very important, automatically enrolling an employee in a plan only overcomes the first hurdle with respect to retirement saving. Employees who are automatically enrolled do not actively engage in the selection of their investments and employers believe that by choosing the most conservative investment option they are protecting themselves from liability. The ultimate result is long-term investments of retirement assets in a money market or other capital preservation fund, even though that is likely not be the best investment strategy.

Plan sponsors and service providers can help participants make better investment choices for their retirement savings by utilizing automatic or managed investing, and default investing options. However, because ERISA Section 404(c) is generally not available unless participants make an affirmative investment election, plan sponsors have been unwilling or unable to use these products. Additionally, retirement plan service providers have been limited in their ability to create and offer automatic and managed investing products because of the cumbersome and arguably unnecessary product design requirements under the current regulatory structure. Specifically, the conflict of interest rules under ERISA and guidance issued by the Department in the Sun America Advisory Opinion<sup>6</sup> generally prohibit service providers from providing investment advice on their own investment products or products they manage.

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<sup>4</sup> Deloitte Consulting LLP 2004 Annual 401(k) Benchmarking Survey.

<sup>5</sup> “*Time May Not Be On Automatically Enrolled Employees' Side*,” Hewitt Associates Press Release (2001).

<sup>6</sup> DOL Advisory Opinion 2001-09A (December 14, 2001). Although guidance issued by the Department in the Sun America Advisory Opinion has been helpful in facilitating the development of some managed investing products for employees, SPARK believes that relief should go further in order to provide plan sponsors with greater ability to use such products. SPARK supports legislation that is consistent with prior legislative proposals regarding this issue, namely the Retirement Security Advice Act of 2003 (S. 1698) and the Pension Security Act of 2003 (H.R. 1000).

SPARK believes that it's critical that the 2006 Summit devote a significant amount of attention to developing policies and programs to leverage inertia and help passive employees save and invest for retirement. Additionally, SPARK believes that the 2006 Summit should devote attention to the advancement of and education regarding changes that (1) protect plan sponsors from fiduciary liability for directing automatic enrollment contributions into a default investment option other than a capital preservation fund, including a managed investing and automatic investing account, provided that (a) plan sponsors act prudently in the selection of the default investment option or the service provider, and (b) the participant has the option to transfer the amounts so invested into another investment option upon request, and (2) allows retirement plan service providers who are investment advisers or who have investment adviser affiliates to provide managed and automatic investing products, and provide individualized investment advice to plan sponsors and plan participants, including advice about the providers' own investment products. To that end, enclosed is a copy of the Statement of Position ("SOP") on Auto Pilot Plans dated June 30, 2005 that SPARK recently submitted to the President, members of Congress, the Department and the Internal Revenue Service. The SOP explains the issues discussed above in greater detail.

## **II. Retirement Income Planning**

For the past twenty-five years, since the beginning of the 401(k)-centric era, individuals and plan sponsors have been focused primarily on the *accumulation* of assets for retirement. Now, as the first generation of baby boomers approach their sixties, these retirees are faced with a new concern that few are prepared to handle. Retirees must decide how to *use* the retirement assets they accumulated and construct a reliable monthly post-retirement income stream that will last over the remainder of their lifetime. SPARK members pay out billions of dollars each year in lump sum payments from retirement plans to individuals who must redeploy those assets into portfolios in order to generate reliable monthly income streams. SPARK believes that it is critical that the 2006 Summit devote a significant amount of attention to developing policies and programs to assist individuals in the transition from the accumulation phase of their retirement planning to the payout phase.

Research data provided by Merrill Lynch shows that on average, Americans expect to be able to continuously withdraw as much as 20% of their retirement savings in each year of retirement, while the average retirement savings per household is less than \$50,000 in total.<sup>7</sup> This data clearly shows that individuals do not understand how much money they need as a lump sum in order to fund a retirement income stream that is at least 70% of their pre-retirement income. Even taking into account potential Social Security and pension plan payments, it is unlikely that the current aggregate savings balances will generate adequate monthly lifetime post-retirement income for most of the baby boomer generation.

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<sup>7</sup> Merrill Lynch 2005 Annual Retirement Survey.

SPARK believes that a greater understanding of the linkage between the retirement savings accumulation phase and the retirement income payout phase could lead to better behaviors among workers. For example, plan participants should understand the significant negative consequences that result when they change jobs and money in retirement savings accounts “leak out” through distribution payments. Today billions of dollars per year are paid out of the retirement system in the form of cash payments to job changers. Education programs and planning tools can be developed and used to help employees estimate and understand the amount of post-retirement income they are giving up with each cash withdrawal over their working life.

Today, only a small percentage of plan sponsors currently offer guaranteed income stream payout options for retiree distributions from defined contribution plans. Having a guaranteed income stream as a payout choice in defined contribution plans can be an important tool in increasing comprehension of the actual expected lifetime income that a participant’s assets can generate. Congress, regulators and the retirement plan industry should work together in order to make guaranteed income stream payout options attractive, cost effective, and administratively practical.

SPARK believes that there are a number of policies and programs that can be put in place to encourage a linkage between pre-retirement savings and potential post-retirement income generation. These programs include (1) guaranteed income stream payout options upon retirement or pre-retirement distributions, (2) guaranteed income stream payout options that are purchased within a plan by the participant during their employment and asset accumulation phase, in effect as an investment option, (3) financial planning tools, (4) personalized retirement account investment management solutions, and (5) educational materials and programs. Public attention to this issue highlighted by an emphasis at the 2006 Summit can play a key role in raising awareness among individuals, employers, and service providers so that solutions can be adopted in time to assist the baby boomers as they begin their retirement years.

### **III. Retirement Plans for Small Businesses**

SPARK members service retirement plans for over two million small businesses across the United States representing almost \$1 trillion in assets. While these numbers are significant, there are still approximately 3.2 million small businesses, or 56%, which do not currently offer a retirement plan to their employees.<sup>8</sup> There are a number of reasons for this lack of penetration in the small business market. According to industry studies, small employers cite the following as important reasons for not offering a plan: (1) concerns over cash flow and revenue, (2) concerns over complexity and liability, and (3) employee turnover.<sup>9</sup> Simplification programs such as SIMPLE plans, and the Economic Growth and Tax Relief Reconciliation Act (“EGTRRA”) tax credit for plan formations have helped promote plan adoption, but these programs still do not address all of the needs cited above.

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<sup>8</sup> U.S. Bureau of Labor Statistics, 2004 Annual Compensation Survey.

<sup>9</sup> EBRI – 2003 Small Employer Retirement Survey.

SPARK believes that there are four courses of action that can be undertaken to encourage more small businesses to adopt retirement programs:

1. provide a legislative and regulatory framework for arrangements that allow multiple employers to band together to adopt a combined plan for all of their employees and allow service providers to provide broad fiduciary services and protection to the participating employers
2. continue to simplify the administration and compliance reporting for small business retirement programs
3. modify safe harbor guidelines for 401(k) plans that would take into account the need for flexible contributions year to year to alleviate employers' concerns about cash flow consistency
4. extend the EGTRRA tax credit to more substantially cover the start up costs of small business retirement plans

Industry trade organizations have approached retirement plan service providers over the years to request an industry “buying co-op” approach to 401(k) plan services that would allow multiple small employers with like businesses to band together to leverage their combined purchasing power for 401(k) plan services and plan investment products. The current legislative and regulatory requirements governing retirement plans do not allow these programs to be offered in an administratively practical and cost effective way.<sup>10</sup>

One of the most significant issues for small employers and retirement plan service providers that are interested in servicing the small plan market is the cost associated with servicing the plans. Small business owners who establish plans are in the business of running a business and generally require more hands on assistance than larger employers with respect to operating a retirement plan. A small business owner's need for greater assistance requires a service provider to devote more resources to servicing the plan. As a result, such plans are more expensive to service and frequently result in the service provider assuming greater responsibility over plan functions. Further complicating this situation is that the cost for plan services must either be paid for by the employer out of business assets or paid from plan account balances, i.e., by plan participants. Small business plans and startup plans generally do not have enough money in them to generate the asset-based fees necessary to compensate a service provider adequately.

Additionally, individual plan trust requirements and fiduciary responsibility regarding investment option selection are significant impediments to the adoption of retirement plans by small businesses. SPARK believes that a “mastertrust” concept could be offered

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<sup>10</sup> Revenue Procedure 2002-21 issued by the Internal Revenue Service (the “Service”) regarding this issue has made small business participation in retirement plans more onerous and complex than necessary. In the Revenue Procedure, the Service concluded that a professional employer organization could not allow individuals other than its own employees to participate in a retirement plan without violating the “exclusive benefit rule” under ERISA, which rule requires an employer to offer a plan only to its own employees. As a result, each professional employer organization was required to set up its own separate plan, or offer a multiple employer plan. Both of these options are cumbersome, inefficient and do not adequately help small business owners reduce their plan costs.

to these types of business co-ops if multiple employers were allowed to commingle funds into a single trust to achieve purchasing power within the investment choices available. Such a program could adopt an “omnibus fiduciary” approach under which a qualified service provider with “approved” investment guidelines accepted collective fiduciary responsibility, thereby minimizing the responsibilities of the small business owner. Similarly, the program could have certain “safe harbor” guidelines that would eliminate the need to perform compliance testing at the individual company level, eliminate the need for individual IRS Form 5500 reporting, and allow for true single plan administration. This approach will provide an administratively practical and cost effective approach that will allow small businesses to offer retirement plan benefits that are similar to those available to larger employers and union plans. SPARK believes that this type of multiple employer approach could be the single most impactful option available to small businesses.

Additionally, according to data from RG Wuelfing, the average up-front out-of-pocket cost to start a retirement plan for an employer is approximately \$3,000. Increasing the amount of the EGTRRA tax credit and extending its availability for a longer time period would make offering retirement plans more affordable for small business owners and encourage greater adoption.

SPARK believes that it’s critical that the 2006 Summit devote a significant amount of attention to developing policies and programs that will help overcome the impediments to better retirement savings opportunities by small business owners and their employees.

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SPARK believes that by focusing attention on the need for automatic retirement savings programs, better retirement income planning, and better and more affordable retirement plans for small businesses the 2006 Summit could have a significant long term impact on American workers’ ability to achieve retirement security and dignity. Substantive regulatory and legislative changes, coupled with proactive industry and public awareness and education campaigns can create the type of seismic shifts necessary to address the impending baby boomer retirement era.

We hope you find these materials informative and helpful. SPARK representatives are committed to playing an active role in the 2006 Summit in order to help make it productive and successful. We are prepared to meet with representatives of the Department to discuss these matters. Additionally, SPARK has access to and is willing

to make available to you extensive research and statistical data regarding the retirement plan industry. Please feel free to call Jeff Close or me at 860-658-5058 if you would like to discuss these matters further.

Sincerely,

Robert G. Wuelfing

cc: Larry H. Goldbrum

Enclosure