STATEMENT FOR THE RECORD

FROM

THE AMERICAN COUNCIL OF LIFE INSURERS

BEFORE

THE 2014 ERISA ADVISORY COUNCIL

ISSUES AND CONSIDERATIONS AROUND

FACILITATING LIFETIME PLAN PARTICIPATION

THURSDAY, AUGUST 21, 2014

Thank you for inviting me to testify this afternoon on the topic of Issues and Considerations Around Facilitating Lifetime Plan Participation. My name is Cynthia Mallett, and I am Vice President for Industry Strategies & Public Policy in the Corporate Benefit Funding division at Met Life. I am testifying today on behalf of the American Council of Life Insurers (ACLI).

ACLI represents more than 300 legal reserve life insurer and fraternal benefit society member companies operating in the United States. These member companies represent over 90% of the assets and premiums of the U.S. life insurance and annuity industry. ACLI member companies offer insurance contracts and other investment products and services to qualified retirement plans, including both defined benefit pension and 401(k) arrangements, and to individuals through individual retirement arrangements (IRAs) and on a non-qualified basis. ACLI member companies also are employer sponsors of retirement plans for their own employees.

ACLI appreciates the Council's balanced presentation of the topic as described in the Issue Statement and the focusing of the discussion to avoid replicating work done by prior Councils (for example, the 2013 examination of pension derisking) and by the Department of Labor (DOL) in its regulatory projects (for example, the definition of fiduciary regulatory project). These issues and IRA rollovers in particular have been the subject of increased scrutiny in recent years. IRAs can serve an important role offering distribution eligible participants a range of investment and distribution options while preserving the tax qualified status of their savings.[1] Likewise, employers can provide new as well as existing and former employees with options that improve their efforts to secure income in retirement.

It is important to distinguish rollovers from leakage. Leakage can have a devastating effect on workers' retirement security. When there is a default on a loan, a hardship withdrawal, or a cash-out (without a subsequent rollover) when changing jobs, the nest egg shrinks.[2]

Employer Considerations

Some plan sponsors focus on retaining retirement assets after separation from service. Keeping participants in the plan can help reduce expenses for all participants by increased economies of scale. On the other hand, some sponsors believe that continued services for former employees, especially when the account balances are modest, is not a good use of plan and company resources. These employers would prefer to distribute accounts of former employees. The preference depends

[1] Note that ERISA provides important protections to participants in employer sponsored DC plans. IRAs are generally not overseen by the DOL. However, many entities focus on consumer protections for IRA owners. For example, IRAs held by insurance companies are subject to the state regulation of insurance. The SEC and FINRA also regulate the sale of registered investments such as mutual funds and variable annuities offered in the IRA market. http://www.ici.org/viewpoints/view_11_ira_regs

[2] Note that various legislators have introduced legislation with provisions to address leakage, most notably, the Shrinking Emergency Account Losses in 401(k) Savings Act of 2013 (SEAL Act), introduced by Senators Nelson and Enzi. Also note the recent Tax Court case, *Bobrow v. Commissioner*, T.C. Memo 2014-21 (including IRS Announcement 2014-15, which addresses how IRS will implement the decision), which may lead to unintentional increased retirement asset leakage. This case clarified that the once-per-year limitation on indirect IRA-to-IRA rollovers (i.e., a rollover made within 60 days of an IRA distribution) applies to any and all IRAs an individual may have. Prior to this case, the IRS applied this rule on a per-IRA basis. IRS Publication 590 still indicates this position. With this ruling and IRS guidance, attempting a second indirect IRA rollover in a 12-month period will lead to a taxable result. While direct, trustee-to-trustee IRA transfers are more common and not affected by this decision, proactive education may be necessary to ensure that individuals will understand the importance of handling rollovers on this basis in order to avoid unnecessary taxable events and retirement asset leakage. We understand that this issue is not within the jurisdiction of the DOL; however, we raise it because it relates to the issues the Council is considering.

greatly on the employer, its finances, the workforce it employs and how it views the role of its benefit plans. For example, when considering whether to include or eliminate provisions that require or encourage former employees with small accounts to take a distribution at termination, employers with high employee turnover may worry that such action could significantly drive down average account size.

Nevertheless, employers should be encouraged to consider whether their plans' provisions, features, or practices discourage former employees from keeping their assets in the plan. For example, the employer should consider whether the plan provides an annuity distribution option.[3]

Employers should be encouraged to assist participants in making informed decisions by educating departing employees about their options. We note that last year, under the Council's topic "Successful Plan Communications for Various Population Segments", the Council spent a great deal of time considering the best ways to educate plan participants as well as the ability to use plan assets for targeted employee communications. As described by the witnesses in the two hearings for that topic, there a number of creative ways that plans can effectively communicate information to their participants.

DOL Interpretive Bulletin 96-1 allows and encourages plans to provide participants and beneficiaries with "general financial and investment information" including materials that inform participants about their "future retirement income needs." ACLI has asked DOL to expand IB 96-1 to explicitly cover retirement income education about distribution options, including lifetime income options.[4] Educational information on rollover options and keeping assets in the plan and the pros and cons of those options should be protected by a comparable safe harbor as investment education on in-plan investments to enable comparable treatment and availability.

Employers often rely on service providers to provide education to plan participants. This is an important service offering that the sponsor is often not equipped to provide itself, and without it, the only information a participant might receive are the documents and notices required by law (summary plan descriptions, etc.). This information should not be discouraged for service providers who have a well-established relationship with the plan sponsor.

<u>Participant Considerations</u>

There are a number of factors to be considered when deciding whether to keep your savings in a plan, rollover your savings to a new employer's plan, or rollover your savings to an IRA (e.g., investment performance of the available investment options net of fees, investment diversification, guaranteed lifetime income options). Fees are not the only consideration.[5]

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[3] Most 401(k) plans do not include an annuity feature. In [ACLI's response](#) to the February 2, 2010 joint DOL and Treasury RFI on Lifetime Income Options, to encourage employers to offer annuity and other guaranteed lifetime income options in plans, ACLI recommended that the annuity selection regulation be revised to modify or eliminate the requirement that fiduciaries make a determination as to whether "an annuity provider is financially able to make all future payments under an annuity contract." In 2012, the ERISA Advisory Council recommended that DOL review, modify, and/or develop regulatory guidance/clarification with respect to decumulation of retirement assets, including a defined contribution plan annuity safe harbor.

[4] Note that prior ERISA Advisory Councils have also made this recommendation to DOL.

[5] http://www.dol.gov/ebsa/publications/401k_employee.html. A participant should "[c]onsider fees as one of several factors in your decision making; [c]ompare all services received with the total cost; and [r]ealize that cheaper is not necessarily better."

In general, employer plans benefit from economies of scale. Thus, it is important for benefit eligible individuals to consider investment performance net of fees when comparing IRAs and their current or future employer's plan. While IRAs can offer a very broad range of investment options, employer plans may include stable value and other investment classes not found in IRAs.

As we note, there are many ERISA defined contribution plans that do not offer any annuity options. We urge the Council to continue to support efforts to facilitate the use of guaranteed lifetime income options in employer plans. It is also important to keep in mind that, with respect to guaranteed lifetime income, IRAs play a key role for today's retirees.[6]

As the Council considers lifetime plan participation, it should keep in mind that the goal is to help Americans save enough throughout their career to provide needed income throughout their retirement. It is important for the Council to recognize that a career may include periods of employment with and without access to an employer sponsored plan. This makes it all the more important for employers to encourage lifetime plan participation. It also raises the important role IRAs can and do play at various points throughout a worker's career.

In addition to investment performance, features and services, there are intangible factors. Some participants may distrust or have negative feelings toward their former employer that leads them to use IRAs or roll their balance to their new employer's plan. Others may wish to stay with their former employer's plan, either for continuity of investment options or as a result of a general mistrust of financial institutions. It is important that the Council recognize that participants want a rollover option, whether or not they utilize it. They need to be able to feel comfortable with their current or former employer's plan or an IRA. This helps to ensure assets stay within the retirement system and not get cashed out.

Because individual circumstances vary, the rules must retain flexibility. Participants' options should be explained rather than constrained and new rules, if any, should facilitate an informed choice on the part of the participant. Participants need education to understand their options and to assist them in making informed decisions. As discussed above under Employer Considerations, employers often rely on service providers, under the employer's supervision, to educate participants in general, including on options upon termination of employment. It is important that this education not be curtailed.

As Mark Iwry, Senior Advisor to the Secretary and Deputy Assistant Secretary for Retirement and Health Policy, US Treasury, testified at the June 17th hearing, employees are provided with a 402(f) notice before taking a distribution. This notice contains information that describes the tax consequences of the different distribution options. In its current form, this notice is lengthy and does not provide a short or easily accessible explanation of participant options. ACLI developed and shared with Treasury a summary 402(f) notice that more clearly summarizes these options including the fact that participants are permitted to leave their money in the plan (See attachment.). As a specific suggestion, this summary could be provided along with the longer 402(f) notice, and could serve to highlight that lifetime plan participation is an alternative for participants.

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[6] Many employer-sponsored defined contribution plans do not currently include an annuity as an in-plan distribution option (see Helman et al (2013, EBRI Issue Brief No. 384) which finds that "just 17 percent of plan participants report that their employer's retirement savings plan currently offers an annuity option"). Thus, plan participants who wish to annuitize some or all of their account balance must rollover their balance to an IRA in order to access the benefits of annuities and guaranteed retirement income options, including longevity annuities described in Treasury's new qualifying longevity annuity contract (QLAC) regulations.

The primary policy goal regarding these issues should be to prevent leakage and to keep assets within the retirement system to be used for the intended purpose, providing for an individual's needs in retirement. Whether the participant decides to leave his balance in the employer plan or roll it to a new employer's plan or an IRA, it is most important that the participant does not cash out his account balance. Employee education about the very serious effects of cashing out is necessary to help counteract the short-term urge to take a withdrawal, especially at a stressful time such as loss of a job. Individuals with lower incomes, lower account balances, and lower financial wealth are more likely to cash out their accounts when they terminate employment.[7] These are the people who are less likely to have access to financial guidance or financial education. Therefore, it is even more important that education be available regarding the options, and the importance of keeping the assets within the retirement system.

We thank you for your consideration of our comments.

[7] See testimony of Sudipto Banerjee, EBRI at the Council's June 17, 2014 hearing.

TAX RULES APPLICABLE TO RETIREMENT PLAN DISTRIBUTIONS

You have at least 30 days to review this information before taking any action regarding your benefits.

SUMMARY

If you elect to receive some or all of your vested account balance directly in **cash**, as a lump sum, a series of payments or as an annuity, the *taxable portion* of any <u>payments made to you will be subject to income tax withholding and includible in your gross income</u>. For payments you receive that are eligible for rollover, *20% income tax withholding applies*. If you receive a payment before age 59½, *you may owe an additional 10% tax*.

You can postpone federal income tax on your retirement savings. When you are eligible for a distribution from a tax-qualified plan, you can defer federal income tax to a later date if you:

- **Leave your benefit in the plan.** If your vested account balance is $5,000 or more and you have not attained the plan's normal retirement age, **the plan may not distribute your benefit without your consent.** A plan may permit you to keep your benefit in the plan beyond the normal retirement age. Please refer to the summary plan description for more information.

  Benefits under $5,000. Depending on the provisions in your plan, if your vested account balance is less than $5,000, it may be subject to automatic cash out. If you do not take action, the plan's administrator may be required to pay you directly or rollover your benefit to a traditional IRA or, for designated Roth amounts, a Roth IRA it establishes for you.

- **Rollover.** If your payment will include amounts <u>eligible for rollover</u>, you may roll the eligible amount over to another plan or to an IRA or Roth IRA. Note that amounts <u>not eligible for rollover</u> include: a series of payments to be made over a number of years; required minimum distributions; hardship distributions; ESOP dividends; and corrective distributions. The plan's administrator will know if all or a portion of your payment is eligible for rollover.

  Direct Rollover. For a rollover to another plan, confirm with the new plan's administrator whether and, if so, how you can accomplish a rollover. For a rollover to an IRA or Roth IRA, the IRA provider or your financial professional can assist you. Your current plan may require you to complete its paperwork to authorize distribution from the plan. Your distribution may be in the form of a check paid to the order of your new plan.

  Indirect Rollover. If you elect to receive payment of an amount that is eligible for rollover, you have up to 60 days from the date of distribution to change your mind and rollover the amount you received as well as the dollar amount that was withheld and sent to the IRS. To roll over 100% of the payment, you must find other money to replace the 20% withheld.