
Law Office of Robert J. Toth, Jr.
110 West Berry Street
Suite 1809
Fort Wayne, IN 46802

O: 260.387.6827
F: 260.449.9771
rjt@rtothlaw.com

**Written Testimony Submitted to
DOL/Treasury Lifetime Income Public
Hearing**

By
Robert J. Toth, Jr.
Law Office of Robert J. Toth, LLC

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I am an attorney in Fort Wayne, Indiana with nearly 30 years of experience in employee benefit matters, with a practice focusing on the development, marketing and distribution of retirement products and services. My background includes experience in the integration of mutual fund and insurance products into retirement plan platforms; designing a process to provide variable annuitization from mutual fund based DC plans; and the application of annuity law to retirement plans. I have published major papers on the legal issues related to providing insurance guarantees from Defined Contribution Plans; and have managed the ERISA legal affairs of a major insurer and served as in-house ERISA counsel to a Fortune 100 company with a billion dollar master trust funding both DB and DC plans with innovative investment arrangements.

As such, I have a unique view of the technical requirements necessary to provide lifetime income from defined contribution plans. The views I herein express are my own, and not of any client.

Today I will address two of the issues related to providing lifetime income from DC plans: the fiduciary issues related to the risk of insurer solvency and the issue of portability of income guarantees. It is worth noting at this time that my

comments address only the technical issues related to enabling DC plans to provide these guarantees. I am not addressing the more fundamental problem related to the failure of many employers to treat the provision of adequate retirement income to their employees as an internalized cost of current employment.

Fiduciary/Insurer Solvency Issue

There are two very different issues related to the risk of insurer solvency where an annuity is purchased to fund lifetime income. The first is a “current state” issue, that is, what should the fiduciary obligations be in selecting an insurer to provide this guaranteed income under the existing regulatory environment. The second issue looks to the future. What should be the appropriate federal policy be with regard to “guaranteeing the guarantor,” as annuities regain widespread acceptance within ERISA plans. Should there be a federally backed ultimate insurance program along the lines of an FDIC, and what should it look like.

Current State

Annuities have a long history of providing retirement income for employees, well before the passage of ERISA. The federal tax system itself has recognized these financial instruments from times predating the 1939 Code. An extensive state-based system of regulation has grown up around these and other insurance products, as the ability to properly protect the pooling of longevity and mortality risk being critical to the welfare of a state’s citizens- risks against which no single purchaser of insurance could ever protect itself. Regulation of reserve levels, investments, contracts, marketing, agent licensing and insurer insolvency all are a part of the system, It is a stable system, one which has not suffered the level of de-regulation that occurred through much of the rest of the financial system has over the past 20 years.

Plan fiduciaries who now choose to allow participants to purchase products to guaranty retirement income through their employer sponsored defined contribution plans should be able to rely upon this regulatory scheme. The DOL should consider recognizing as prudent a fiduciary’s reliance on the state’s regulatory schemes; no fiduciary could adequately protect a plan against the future insolvency of an insurance carrier. To require fiduciaries to a higher standard of care than what is otherwise possible would be in contradiction to the ERISA standard of care, which relies upon “the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims.”

The current state regulatory system could be viewed as be flawed in certain important respects, flaws which could lead to unprotected participants and even abuse if such a broad standard is adopted without some other protective measure. This additional protection could be based readily available, current and objective financial information. For example, a fiduciary safe harbor could give deference to reliance on the state regulatory scheme (on insolvency risk) if the insurer is otherwise rated at or above a certain chosen rating by one or more recognized rating agencies. Using specific ratings have limited value as a true differentiator of quality of an insurer itself can create fiduciary problems. However, reliance upon broad ratings brackets instead of specific ratings helps avoid the difficulties inherent in rating systems, while taking advantage of the benefits they do provide.

Note that this relief would only apply to the insolvency risk. The fiduciary would still need to perform its diligence with regard to the suitability, design and price of the annuities being purchased.

Future State

Beyond the immediate question of the standard to which plan fiduciaries will be held for insurance company insolvency is the larger (and separate) question of whether the existing system should be replaced or supplanted with something else.

The current system which protects insurance policyholders from insurer insolvency is the state guaranty association system, which is the final step backing an entire regulatory process. Each state maintains its own program, generally in accordance with uniform laws which have been developed through the NAIC. These associations are not funded; they instead rely on assessments upon other insurance companies in the domicile state of the insolvent insurance company. It has the appearances of an ad hoc system subject to a number of varying limitations, but it is also one in which the guaranty associations have made substantial efforts at coordination.

Addressing the limitations and weaknesses of the process, and developing a uniform program well suited for ERISA plans under which the purchase of insurance guarantees are an integral part of the system, is something which will take time consuming analysis and legislation.

Answering this question is separate than that of what the fiduciary standard should be in the current environment, and should not prevent the application of the interim standard described above.

Portability

Portability, at first glance, seems to be one of the more intractable issues to resolve in the efforts to make lifetime income products easily available from defined contribution plans. It includes both the ability to preserve a guarantee already purchased and the ability to consolidate guarantees collected over a lifetime. It is a critical element of a successful retirement income program, given the mobility of the workforce; the life cycle of corporate employers/plan sponsors; and the fiduciary obligation to be able change current issuers of guarantees in plans.

The challenge of preserving the guarantees, which have purchased and the ability to consolidate them at retirement have been well addressed over a long period of time in the retirement marketplace and the associated federal regulatory scheme. It is just that these concepts have never been widely applied, nor are familiar, to the 401(k) marketplace, where the vast majority of defined contribution assets reside. The task will be to find a manner to effectively update and “bridge” these existing rules to help accommodate the needs of adequate retirement security.

I specifically refer to the development and regulation of Individual Retirement Accounts and Annuities under Code Section 408; pre-2007 403(b) annuities, as applied outside of the employment context; defined benefit terminal funding annuities; and the use of the qualified plan distribution annuities. Each of these arrangements are effectively “individual pensions,” with the underwriters and issuers of these products having tax compliance responsibility for the applicable rules. In addition to the individual being able to maintain his or her guarantees in a compliant environment, transfers and consolidation between them have been well accommodated in the past through the use of 1035 exchanges and (before its repeal) 90-24 exchanges.

The application of a number of these existing rules will need to be clarified and extended to all types defined contribution plans by regulation or ruling, but the basic structure currently exists to accommodate these products.

These rules address the distribution of guarantees from a plan upon a distributable event, where a participant has purchased the guarantees as part of the distribution from the plan, or takes a distribution of the guarantees previously purchased. Experience is now telling us, however, that legislative change is likely necessary for the accommodation of those products under which a participant accumulates various sorts of guarantees as an investment in defined contribution plans during employment, through the use of elective deferrals. This can create a challenge for plan sponsors and record keepers when the plan discontinues its relationship with the issuer of the guarantee. Sponsors and administrators will be still be required to report on these guarantees, under these circumstances, until the participant has a distributable event. A legislative option would be to treat these guarantees as being distributed as individual pensions as long the vendor meets certain requirements and takes on certain compliance responsibilities. This would include, but not be limited to, meeting substantial transparency and suitability requirements. If the vendor could not meet those requirements, then those products could not be distributed in this manner.

In close, retirement plan products have a long history of providing income guarantees to retirees-well predating the growth and reliance upon the 401(k) plan. As we seek to enable the defined contribution system to help accommodate for the inadequacies of the existing defined benefit system, it should be recognized that substantial structures already exist at both the federal and state level, which can be utilized as the basis for this effort.