Annuity Junk Fees in Current 401(k) Plans

By Chris Tobe, CFA, CAIA

I want to applaud the Biden Administration on bringing Annuity Junk fees into the light of day to protect investors.   This rule is an important first step.   Bowing into industry pressure to enrich annuity salesmen would do much harm to investors.

I want to focus on the effect of Annuity Junk fees in Current ERISA protected Defined Contribution plans (*401(k) and 403(b)*   While the White House release mentions the savings in current plans from Index annuities, I think that fixed annuities savings could be much larger over $9 billion a year.   (*It is important to note that fixed annuities and index annuities in Government Defined Contribution plans in both 457 and 403(b) are not protected by ERISA and add to many more $billions.*)

My $9 billion a year comes from industry figures on General Account Fixed annuities at $386 billion and Separate Account Fixed Annuities at $76 billion in ERISA Defined Contribution Assets. [i]

However, it is important to note that the largest provider of Fixed Annuities in Defined Contribution plans (governed by ERISA) is TIAA, which has substantially lower fees and commissions, than the other mainstream insurance providers

Fixed Annuities for the most part do not disclose fees and are rate based. For example, when a similar competitive fixed annuity in a plan like TIAA pays 7% many insurers only pay 2% - pocketing the spread. Bloomberg quoted an insurance executive bragging about these hidden 2%+ in fees at a Wall Street conference.[ii] These hidden spread fees have the same negative effect on investors that disclosed mutual fund fees have.

HOW DO I KNOW THIS

I currently consult on excessive fees in insurance products.   I spent 7 years making insurance products for Transamerica Life one of the largest U.S. insurance companies. I was an officer of 7 different TA companies governed by 4 different states. I saw the need for federal intervention as insurers had the ability to select the state regulator with the loosest regulations and lowest capital requirements.

RISKS

One of the most basic fiduciary principles is diversification. Annuities make a mockery of this principle with their single entity credit and liquidity risk. [iii]

After the first Annuity risk crisis in 1992 the Federal Reserve wrote a major paper on the weakness of state regulations in the insurance area. [iv]

In 2008 Federal Reserve Chairman Ben Bernanke said about these annuity products *"workers whose 401(k) plans had purchased $40 billion of insurance from AIG against the risk that their stable-value funds would decline in value would have seen that insurance disappear."*[v] Even when the Federal Governments step up to control risk in annuity products after the 2008 financial crisis, the insurance industry used it immense lobbying ability to thwart regulations and maximize profits. [vi]

ACCOUNTABILITY

In light of recent money market rates of over 5% these low 2-3% annuity rates in 401(k)'s in far riskier products are especially troubling, costing investors $billions in retirement savings while taking much higher risks.

Hopefully these junk fee rules will slow the growth of these high fee high risk products inside of 401k plans. The latest con game is selling annuities under the guise of Guaranteed Income. [vii]

Hopefully this junk annuity initiative will expose some of the 401(k) target date funds which are burying index and fixed annuities inside weakly state regulated Collective Investment Trusts (CIT)s. [viii]

Hopefully 401(k) consultants who claim to be somewhat independent will be exposed by showing how they use their insurance licenses for additional backdoor commissions.[ix]

Hopefully within 401(k) plans they will either replace fixed annuities with diversified lower risk synthetic stable value products or at the minimum pay competitive rates like TIAA. [x]

This Biden Annuity Junk Fee initiative will save retirement investors billions. Please do not let the Insurance Industry water it down to line their own pockets.

Chris Tobe, CFA, CAIA is a national expert on excessive fees in retirement plans. He has written 4 books and dozens of articles on transparency, excessive fees & corruption in investments. His own firm Tobe Consulting has advised on over 70 ERISA legal cases on behalf of investors who have lost money through risky and/or high fee investments. He serves as Chief Investment Officer for a minority woman owned pension consulting firm out of New Orleans the Hackett Robertson Tobe group

----

[i] **. https://www.stablevalue.org/stable-value-at-a-glance/**

[ii] **https://www.bloomberg.com/news/articles/2013-03-06/prudential-says-annuity-fees-would-make-bankers-dance#xj4y7vzkg**

[iii] **https://commonsense401kproject.com/2022/05/11/annuities-are-a-fiduciary-breach/**

[iv] **Federal Reserve Bank of Minneapolis Summer 1992 Todd, Wallace SPDA's and GIC's http://www.minneapolisfed.org/research/QR/QR1631.pdf**

[v] **Eleanor Laise, " 'Stable' Funds in Your 401(k) May Not Be," Wall Street Journal , March 26, 2009. Available at http://online.wsj.com/article/SB123802645178842781.html**

[vi] **https://www.stanfordlawreview.org/online/the-last-sifi-the-unwise-and-illegal-deregulation-of-prudential-financial/**

[vii] https://commonsense401kproject.com/2022/02/10/401k-lifetime-income-a-fiduciary-minefield/

[viii] https://commonsense401kproject.com/2022/06/07/toxic-target-date-case-study-of-the-worst-of-the-worst/

[ix] **https://commonsense401kproject.com/2022/03/09/conflicted-401k-consultants-should-plan-sponsors-fire-them-sue-them-or-both/**

[x] https://commonsense401kproject.com/2022/02/28/stable-value-the-goood-the-bad-and-the-ugly-avoiding-litigation/