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## Panelists Ponder Future DC Plans



Doug Goodman

**Questioning:** Participants in P&I's round table were, clockwise from from top left, Richard A. Davies, Dallas Salisbury, David L. Wray, Karen Friedman, Stephen W. McCaffrey and Michael A. Sasso.

## P&I round table discusses problems surrounding annuities and other issues facing industry

By **Jeff Nash**, *Pensions & Investments*  
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Annuities as an investment option in defined contribution plans have legal and fiduciary hurdles to overcome before there's any chance they will become commonplace, members of a *Pensions & Investments* round table warned.

The panelists also agreed use of automatic enrollment will continue to increase, despite the topic's absence from President Barack Obama's most recent budget. They also tackled the thorny issue of what should be done to ensure target-date funds have appropriate equity exposures.

The round table was held May 18 in New York. Panelists were: Richard A. Davies, head of product strategy at AllianceBernstein Defined Contribution Investments, New York; Karen Friedman, policy director, Pensions Rights Center, Washington; Stephen W. McCaffrey, senior counsel at National Grid U.S., Brooklyn, N.Y.; Dallas Salisbury, president and chief executive officer, Employee Benefit Research Institute, Washington; Michael A. Sasso, principal at consultant Portfolio Evaluations Inc., Warren, N.J.; and David L. Wray, president,

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the Profit Sharing/401k Council of America, Chicago.

The annuities issue has become red hot. Last month, Putnam Investments CEO Robert Reynolds called for a national insurance charter and an FDIC-like fund to back up lifetime guarantees as part of a sweeping list of proposals aimed at fixing DC plans. And Mark Iwry, who in April was appointed by Treasury Secretary Timothy Geithner as senior adviser and deputy assistant secretary for retirement and health policy, is researching the idea and plans to publish his findings as early as July.

“I think one of the top goals of the new (Obama) administration is to find a way to annuitize or at least guarantee or secure some sort of income in retirement,” said Mr. Davies. “That’s really the final piece of the DC puzzle.”

But making that piece fit will be difficult, panelists agreed. For starters, Congress would need to repeal the joint and survivor annuity laws, which allows a non-employee spouse the right to choose a survivorship annuity as the way in which benefits are distributed from the plan, Mr. Wray said. The problem with the laws, he explained, is that when such an option is offered, men are disadvantaged by having to use gender neutral annuitization. Instead, men would get a much better deal by rolling over their 401(k) account and then buying an annuity based on the men-only mortality table.

“I know that one very prominent company has an annuity purchasing program in their plans, and I can tell you right now, they do not have the blessing of the federal government,” said Mr. Wray. “The problem is we have to change the law in order to get the kind of flexibility that the system needs.” Added Mr. Salisbury: “You can find lawyers all over the map on whether any of these annuity products can technically be put into the QDIA” — qualified default investment alternative.

Mr. Sasso noted that adding annuities poses the fiduciary issue of selecting an insurance company that will be solvent in the decades ahead. “Where does the law start and stop when it relates to the fiduciary exposure by putting your employees into an insurance company that may or may not fail?” he asked. “We have to concern ourselves with the fiduciary aspects of offering annuities and what impact that may have down the road with fiduciaries of qualified plans.”

Ms. Friedman said many employees and retirees are worried about “less than stable” insurance companies. “Even if the benefits are insured by the state insurance funds, those are limited,” she said. “And so Bob Reynolds’ idea of having a federally backed insurance fund has some appeal. But then again, you might be insuring companies that are unstable. So it’s problematic.”

Another hurdle, Ms. Friedman said, is making annuities a decent option for women. “If women go into a private market to buy an annuity, they’re going to get a lot less than men because it’s sex-based annuities. Insurance products are still expensive, so we would have to look at ways of controlling costs and also (increasing) transparency.”

She also said that convincing 401(k) participants with account balances of \$100,000 or less to give some por-

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tion of their retirement savings to an insurance company would be difficult.

Mr. McCaffrey agreed that plan participants have been reluctant to use annuities. “I was with an employer who had annuities in their plan for 10 years and ultimately decided to take it out because it was used less than 1% of the time,” he said. “Nobody wanted to use it. Everybody wanted to take their 401(k) lump sum and go do with it how they saw fit, whether it was buying a boat or rolling it over into an IRA and diversifying an account. People just didn't take up on the annuity.”

## **Target-date connection**

Because more plan sponsors are encouraging participants to stay in their plans after retirement, the idea of adding annuities will tie into how companies structure their target-date funds, explained Mr. Davies. “I think the flexibility of the guaranteed withdrawal benefit — getting it in as part of the target structure five, 10 years out before retirement and then taking somebody seamlessly through and encouraging them to stay in the plan — that's a more interesting model that's worthy of exploration than the traditional lump sum, go to a financial adviser and get advice on a rollover.”

As for Mr. Reynolds' call for an FDIC-like federal backup program for annuities, Mr. Salisbury argued that without such a program, Congress won't “ever do anything to seek to increase annuity use in defined contribution plans or to default it in any way.”

Ultimately, Mr. Salisbury said, it will take an economic recovery to support the acceptance of annuities for 401 (k) plans. “We need a dramatic insurance company confidence recovery,” he said. “Trust will have to come back to financial institutions and insurance companies in particular.”

More companies also are likely to implement automatic enrollment as the economy recovers, the panelists agreed. “It's going to take four or five years for this to spread into the smaller companies, but the future is bright,” said Mr. Wray. “We need to get through the current (economic) situation. Companies are not changing their plans at this point.”

The speakers stressed, however, that companies need to better communicate to employees the need to increase their deferral rate, either on their own or through a company's automatic-escalation program, in which the deferral rate is increased automatically. “Putting somebody in at a 3% rate when they first come in (and then leaving it unchanged) for their career, they probably won't have the understanding that they are going to need to up that nine or 10 percentage points so they can retire comfortably,” said Mr. McCaffrey.

Mr. Davies agreed: “I think people are being auto-enrolled at too low a level. If you're going to enroll people at 3%, to not have auto escalation is really doing them a disservice.”

In discussing the brouhaha over the equity exposure of target-date funds designed for people at or near retirement age, Mr. Davies said: “I think we are nervous that there's some talk of regulating what the appropriate asset allocation would be.” His employer, AllianceBernstein, is a target-date fund provider. “But there are procedures under ERISA, at least in the private sector, that give responsibility appropriately to plan sponsors to make the decisions for themselves.

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