INSURED RETIREMENT INSTITUTE

February 14, 2024

Submitted via Federal e-Rulemaking Portal at: (www.regulations.gov)

Natalia Li, Director
Office of Consumer Policy
United States Department of the Treasury
1500 Pennsylvania Ave. NW
Washington, DC 20220

RE: Request for Information on Financial Inclusion, Agency/Docket Number: TREAS-DO-2023-0014, Document Number: 2023-28263

Dear Director Li:

On behalf of our members, the Insured Retirement Institute ("IRI")[1] appreciates the opportunity to provide these written comments to the U.S. Department of the Treasury (the "Department") regarding the Request for Information on Financial Inclusion (the "RFI").

Many workers and retirees across our nation lack access to or are not positioned to fully utilize the financial system to successfully build both short-term stability and long-term financial security. When groups of people and communities are underserved by existing financial frameworks, they often lag far behind in the accumulation of retirement savings and participation in employer-sponsored retirement plans.

To advance greater diversity, equity, and inclusion (DEI) among those participating in the private-sector retirement system and improve their prospects for financial security in retirement, IRI was proud to support the inclusion of a measure in the *Fiscal Year 2023 Financial Services and General Government Appropriations Act* (Public Law 117-328, Div. E) directing the Department to develop a national strategy to broaden access to financial services for underserved communities. This measure called for national objectives for financial inclusion benchmarks for measuring progress and offered recommendations for how public policy, government programs, financial products and services, technology, tools, and infrastructure can enhance financial inclusion.

IRI believes that the legislative measures referenced below, if enacted by Congress, would promote financial inclusion and provide access to savings and services to historically underserved communities – including people of color, women, and people with disabilities. IRI supports and advocates for the enactment of the following common-sense, bipartisan policies to help all workers and retirees achieve economic equity, strengthen their financial security, and protect their income to sustain them throughout their retirement years.

[1] The Insured Retirement Institute (IRI) 'is the leading association for the entire supply chain of insured retirement strategies, including life insurers, asset managers, broker-dealers, banks, marketing organizations, law firms, and solution providers. IRI members account for 90 percent of annuity assets in the U.S., including the foremost distributors of protected lifetime income solutions, and are represented by financial professionals serving millions of Americans. IRI champions retirement security for all through leadership in advocacy, awareness, research, and the advancement of digital solutions within a collaborative industry community. Our members support and advocate for common sense, bipartisan policies to help America's workers and retirees achieve their retirement goals by expanding access to professional financial guidance and lifetime income products within an appropriate and effective consumer protection framework.

The policy proposals supported by IRI that are most relevant to the RFI are policies that would expand opportunities to save for retirement, foster innovation and modernization of services, and boost diverse representation within the retirement income industry.

Expand Opportunities to Save for Retirement

Require Employers to Offer Retirement Plans to Employees

Nearly half of America's workers are employed by companies that do not offer a traditional pension or a retirement savings plan. Most of these workers are employed by small businesses, with 48 percent of small business employees not having access to retirement plans.[2] In addition, there are disparities by race and ethnicity among those workers, with nearly 64 percent of Latino workers, 53 percent of Black workers, and 45 percent of Asian American workers lacking access to an employer-provided retirement plan.[3]

To provide more workers with opportunities to access a workplace retirement plan and increase their retirement savings, Congress should enact legislation such as the ***Automatic IRA Act of 2024*** (**H.R.7293-118th Congress**), which would generally **require all but the smallest of employers to maintain an automatic retirement savings plan, into which employees would be automatically enrolled with the ability to opt out.** A recent study of the impact of such a new law on workers' retirement security found that over the next ten years, $7 trillion in additional retirement savings would be generated, and 62 million new retirement savers would be created, 98% of whom earn less than $100,000 per year, including 7 million new Black savers and 10.8 million new Latino savers.[4]

This legislation will also create retirement savings opportunities for the 73.3 million American workers[5] who participate in the gig economy by directing the Secretary of the Treasury to **issue regulations or other guidance to provide for making workplace retirement plans available to individuals who provide services to an employer that do not constitute employment.** The legislation will also help address the anxiety felt by many of America's workers about outliving their retirement savings by **requiring that participants with account balances of $200,000 or more be given the choice to receive up to 50% of their vested balance in the form of protected, guaranteed lifetime income products**.

Allow Catch-Up Contributions for Qualified Caregivers

Every year, an increasing number of workers leave the workforce, often for multiple years, to provide full-time care to a dependent family member. While this is a noble decision, it is often the only option they have when seeking to provide the care needed for their family member. As a result, not only is the worker's income eliminated for the time they are giving care, but their ability to participate in employment-based retirement savings plans is also lost. The challenge of leaving the workforce to care for a family member disproportionately impacts women, according to the Bureau of Labor Statistics, which reported that women make up 58% of the 40.4 million people providing full-time care to a family member.[6] This disproportionate

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[2] "Fact Sheet: Final Rule on Association Retirement Plans (ARPs)," U.S. Department of Labor, July 2019.
[3] "Studies Spotlight Racial, Ethnic Gaps in Retirement Savings," AARP, July 2022.
[4] Letter of Support Retirement Subtitle "Build Back Better Act, Page 2, Footnote #s 3-5, ARA, September 2021.
[5]"The State of Gig Work in 2021," PEW Research Center, December 2021.
[6] "Unpaid Eldercare in the United States," Bureau of Labor Statistics. November 2019.

impact is further illustrated by recent reports that found women have between one-third[7] and two-thirds[8] less savings than the median retirement account balance of men.

To address the challenges faced by workers who have left their jobs to serve as caregivers, Congress should enact the ***Expanding Access to Retirement Savings for Caregivers Act*** (**H.R. 6772-118th Congress**), which would **provide qualified caregivers the opportunity to make catch-up contributions for a period equal to their time spent as a caregiver before reaching age 50**. This change would allow caregivers to make up for the lost time in accumulating savings for their retirement when they are able to return to the workforce and aid them in getting back on a path to a financially secure retirement.

Further, Congress should consider additional legislation that would **enable individuals who certify that they were unable to work due to providing care to a family member to become eligible to make contributions of up to the contribution limit into a Roth IRA while being subject to Roth IRA income limits and without having compensation**.

Decrease the Age for Participation in Workplace Retirement Plans to 18 Years of Age

College enrollment rates for recent high school graduates have declined by 21 percent year-over-year as younger Americans weigh the cost of obtaining a higher education versus pursuing technical training and apprenticeships as paths toward a sustainable career.[9] As a result, more young people are beginning their careers earlier. In doing so, they are challenged to start building their retirement nest eggs, because current law limits the number of young people who have access to their employer's sponsored retirement savings plan. A recent study showed that 60 percent of employers were found to not offer benefits to their employees younger than 21 years of age.[10]

Congress should enact legislation, such as the ***Helping Young Americans Save for Retirement Act*** (**S.3305-118th Congress**). The bill would enable more young workers to access employer-sponsored retirement savings plans by **reducing the age of participation in an ERISA-covered defined contribution plan to 18.** The bill would also **reduce costs for employers who offer participation in their workplace plans to younger workers**, making it more advantageous for an employer to do so. Lowering the participation age to 18 will expand opportunities for younger workers to save for retirement by providing them with an additional three years to begin saving and take advantage of the growth offered by compounding interest.

Foster Innovation and Modernization of Services

Streamline How Consumers Receive Electronic Documents

Technology has become dramatically more available and reliable in the past twenty years since the most recent laws governing electronic communications for commerce were enacted. Congress should enact legislation, such as the ***E-SIGN Modernization Act*** (**S.3715-117th Congress**), which would **streamline how**

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[7] "Closing the Gender Retirement Gap." T. Rowe Price. March 2023
[8] "The Four Pillars of New Retirement: What a Difference a Year Makes." Edward Jones. June 2021
[9] "College Enrollment & Student Demographic Statistics." Education Data Initiative. January 2024.
[10] "Advocacy Update – What's Next in 2023." American Society of Pension Professionals & Actuaries. June 2023.

consumers receive electronic communications by removing outdated requirements and ensuring retirement savers can continue to choose how they want to receive and access their financial information.

Additionally, the U.S. Securities and Exchange Commission (SEC) recently rescinded substantial applicability of Rule 30e-3, which had previously allowed for the electronic delivery of certain shareholder reports. To correct this change, Congress should consider legislation, such as the ***Improving Disclosure for Investors Act*** (**H.R.1807-118th Congress**), which would **direct the SEC to write a rule permitting electronic delivery of required reports for all registered investment companies.** By enabling plan notices, statements, and reports to be delivered electronically, non-native English speakers and those who are blind or have other disabilities will be able to take advantage of modern technologies to ensure they are able to access information relating to their retirement savings.

Authorize the National Use of Remote and Electronic Notarizations

The COVID-19 pandemic dramatically changed how consumers go about their daily lives and conduct business. Social distancing measures and virtual meetings became available to combat the spread of the virus, and many businesses adopted digital solutions. However, various laws and rules applicable to the insured retirement industry require individuals to be physically present to conduct business and access the products and services needed to prepare for retirement. As federal and state regulators responded to the pandemic by authorizing temporary relief measures, it became clear that the use of virtual meetings, signatures, and notarizations was a safe and effective manner of conducting business.

It would benefit consumers to make those interim measures permanent – particularly for those with disabilities or other contributing factors that make leaving the home a challenge. Congress should enact legislation, such as the ***Securing and Enabling Commerce Using Remote and Electronic Notarization Act*** (**H.R.1059**/**S.1212-118th Congress**), which would **establish minimum federal standards for the nationwide use of remote online notarizations and ensure that all 50 states, the District of Columbia, and territories of the United States recognize the use of current technologies for notarizations and essential transactions executed in the conduct of interstate commerce and provide easier access to services to those who require it.**

Boost Diverse Representation within the Retirement Income Industry

Enhance Corporate Governance by Increasing Diverse Representation

While the insured retirement industry is committed to improving access to retirement savings, protected, guaranteed lifetime income solutions, and financial services for America's workers and retirees to help reduce racial and gender wealth gaps, the industry also recognizes that improvement is needed in terms of diversity, equity, and inclusion within the industry's leadership and workforce. Studies show that more inclusive workforces produce greater innovation, improved decision-making, more opportunities for professional growth, and increased access to new markets.[11]

[11] "Why Diversity and Inclusion Are Good for Business." University of North Carolina, Pembroke. October 2021.

To support and encourage the industry's efforts in this space, Congress should enact legislation, such as the ***Improving Corporate Governance Through Diversity Act*** (**S.2007**/**H.R.4177-118th Congress**), that would **require organizations regulated by the SEC to file annual reports disclosing the gender identity, ethnicity, sexual orientation, and veteran status of their board of directors, nominees to their boards, and senior executive officers.** Disclosure of such information will provide a transparent look at a company's steps to advance diversity, equity, and inclusion (DEI) practices. Achieving DEI goals and the enhancements brought to the table by a diverse workforce will also help the industry better serve under-represented communities and position America's workers and retirees to achieve a financially secure retirement.

DOL's 2023 Fiduciary Proposal Runs Counter to Promoting Greater Financial Inclusion

The common-sense legislative solutions described above would bolster a national strategy to enhance access to savings and services to build financial security for more of America's workers and retirees. However, a recent rule proposal from the Department of Labor (DOL) threatens to undermine the meaningful steps that Congress, and the Department have taken to make our financial system more broadly inclusive.

On October 31, 2023, the President publicly announced a proposed DOL rule titled ***Retirement Security Rule: Definition of an Investment Advice Fiduciary*****.** The "one-size-fits-all" "fiduciary-only" approach taken by the DOL in this proposal will harm millions of Americans – particularly lower- and middle-income retirement savers – by making it harder, and in many cases impossible, to access professional financial guidance and lifetime income solutions.[12] This proposal is functionally equivalent to a rule adopted by the DOL in 2016. When the 2016 rule went into effect, 10.2 million retirement savers lost access to essential financial advice through their brokerage accounts.[13] Fortunately, the Fifth Circuit Court of Appeals vacated the 2016 rule, mitigating the damage done to retirement savers at that time.

In 2021, Quantria Strategies[14] conducted a study to determine the economic impact of the DOL's continued pursuit of a fiduciary-only approach. Among the study's findings was the startling revelation that adoption of a proposal substantially similar to the 2016 rule would result in a disproportionate reduction in the retirement savings of our nation's Black and Hispanic populations – resulting in a 20 percent increase in the racial wealth gap over a 10-year period. The DOL has not addressed this evidence that the proposal will harm people of color, nor does it present any evidence to the contrary (or, for that matter, any evidence that changes to the existing regulatory framework governing the conduct of financial professionals are even necessary at this time).

In 2015, 93 Democratic Members of Congress, 54 of whom still serve in the House and three of whom now serve in the Senate, sent a letter expressing similar concerns to the DOL in response to the proposal that ultimately became the 2016 rule. Specifically, the letter urged the DOL to ensure that its rule "does not limit consumer choice and access to advice, have a disproportionate impact on lower- and middle-income communities, raise the costs of saving for retirement […] or disadvantage lifetime income options."[15] The

[12] For additional details, please see IRI's comment letter submitted to the DOL on January 2, 2024, which is attached to this letter as Appendix A.
[13] "The DOL Fiduciary Rule: A study on how financial institutions have responded and the resulting impacts on retirement investors." Deloitte. August 2017.
[14] "Analysis of the Effects of the 2016 Department of Labor Fiduciary Regulation on Retirement Savings and Estimates of the Effects of Reinstatement." Quantria Strategies. November 2021.
[15] A copy of this letter is attached hereto as Appendix B.

concerns raised in the House Democrats' letter were not addressed in the final 2016 rule, nor are they addressed in the 2023 rule proposal. Leaving these concerns unaddressed is to the detriment of individuals of all races, and particularly for Black and Hispanic people looking to participate in the financial system and secure their financial futures. Adopting the 2023 proposal would represent a significant step backwards in pursuing a more inclusive financial system. IRI has called for its withdrawal in comments submitted to the DOL on January 2, 2024.

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IRI appreciates the opportunity to share our recommendations for actions to enhance inclusion in the financial system and our concerns about how the DOL's proposed rulemaking would run counter to and significantly impair the efforts of the Department and the President to develop a national strategy to provide all of America's workers and retirees with access to the financial products and services they can use to achieve their financial goals. IRI and our members stand ready to support and assist the Department in this critically important endeavor. Please let us know how we can help or if you have any questions about any of the information provided in this letter.

Sincerely,

Jason Berkowitz
Chief Legal and Regulatory Affairs Officer
Insured Retirement Institute

Paul J. Richman
Chief Government and Political Affairs Officer
Insured Retirement Institute

APPENDIX A

<u>Submitted Through the Federal eRulemaking Portal</u>

January 2, 2024

Office of Regulations and Interpretations
Employee Benefits Security Administration
Room N–5655
U.S. Department of Labor
200 Constitution Avenue NW
Washington, D.C. 20210
Attn: Definition of Fiduciary-RIN 1210–AC02

Office of Exemption Determinations
Employee Benefits Security Administration
Suite 400
U.S. Department of Labor
200 Constitution Avenue NW
Washington, D.C. 20210
Attn: D–12057, D–12060, and D–12094

Re: Retirement Security Rule: Definition of an Investment Advice Fiduciary
RIN 1210-AC02

Proposed Amendment to Prohibited Transaction Exemption 2020-02
Application No. D–12057, RIN 1210-ZA32

Proposed Amendment to Prohibited Transaction Exemption 84-24
Application No. D–12060, RIN 1210-ZA33

Proposed Amendment to Prohibited Transaction Exemptions 75-1, 77-4, 80-83, 83-1, and 86-128
Application No. D–12094, RIN 1210-ZA34

To Whom it May Concern:

On behalf of our members, the Insured Retirement Institute ("<u>IRI</u>")[1] appreciates the opportunity to provide these written comments to the Employee Benefits Security Administration ("<u>EBSA</u>") of the U.S. Department of Labor (the "<u>Department</u>") regarding the proposal titled, Retirement Security Rule: Definition of an Investment Advice Fiduciary, and the associated proposals to amend certain prohibited transaction exemptions (collectively, the "<u>Proposal</u>").

For the reasons presented below, IRI urges the Department to withdraw the Proposal and to discontinue this rulemaking project unless and until there is objective data and evidence of actual harm to retirement savers that cannot be effectively addressed under current rules.

[1]The Insured Retirement Institute (IRI) is the leading association for the entire supply chain of insured retirement strategies, including life insurers, asset managers, broker-dealers, banks, marketing organizations, law firms, and solution providers. IRI members account for 90 percent of annuity assets in the U.S., include the foremost distributors of protected lifetime income solutions, and are represented by financial professionals serving millions of Americans. IRI champions retirement security for all through leadership in advocacy, awareness, research, and the advancement of digital solutions within a collaborative industry community.

From the outset, we want to be clear that we are not requesting, recommending, or proposing modifications to any of the components of the Proposal.[2] We do not believe the Proposal can or should be "fixed," and nothing in this letter should be read to suggest or imply that IRI would support a modified version of the Proposal. Instead, our comments are intended to explain the myriad reasons why the Department should withdraw the Proposal and discontinue this regulatory project.

Rules that deprive retirement savers of access to protected lifetime income products and the professional guidance they need to knowledgeably acquire and use those products run counter to the best interests of American workers. There is extensive evidence that the regulatory package adopted by the Department in 2016 (the "2016 Rule")[3] and vacated by the Fifth Circuit Court of Appeals in 2018 (the "Chamber Decision")[4] resulted in significant harm to retirement savers[5] and that the adoption of similar rules will have the same result, if not worse – especially for lower- and middle-income savers and underserved communities.[6] IRI's opposition to the

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[2] The Proposal is comprised of four components: (i) Retirement Security Rule: Definition of an Investment Advice Fiduciary (RIN 1210-AC02) (the "Fiduciary Definition Proposal"); (ii) Proposed Amendment to Prohibited Transaction Exemption 2020-02 (Application No. D–12057, RIN 1210-ZA32) (the "2020-02 Proposal"); (iii) Proposed Amendment to Prohibited Transaction Exemption 84-24 (Application No. D–12060, RIN 1210-ZA33) (the "84-24 Proposal"); and (iv) Proposed Amendment to Prohibited Transaction Exemptions 75-1, 77-4, 80-83, 83-1, and 86-128 (Application No. D–12094, RIN 1210-ZA34) (the "Other PTEs Proposal" and together with the 2020-02 Proposal and the 84-24 Proposal, the "PTE Proposals"). References to the "Proposal" in this letter are intended to refer to the Fiduciary Definition Proposal and the PTE Proposals collectively.

[3] The 2016 Rule was comprised of: (i) amendments to the definition of "investment advice fiduciary" under the *Employee Retirement Income Security Act of 1974*, Pub. L. No. 93-406, 88 Stat. 829, codified as amended at 29 U.S.C. § 1001 et seq ("ERISA"), and the *Internal Revenue Code*, 26 U.S.C. § 4975 (the "Tax Code"), (ii) amendments to six existing administrative exemptions from the prohibited transaction rules imposed under ERISA and the Tax Code ("PTEs"); and (iii) two new PTEs. *See* 81 FR 20946, 81 FR 21002, 81 FR 21089, 81 FR 21139, 81 FR 21147, 81 FR 21181, and 81 FR 21208.

[4] *Chamber of Com. of U.S. of Am. v. U.S. Dept. of Lab.,* 885 F.3d 360 (5th Cir. 2018) ("Chamber Decision").

[5] U.S. Chamber of Commerce, *The Data Is In: The Fiduciary Rule will Harm Small Retirement Savers* (Spring 2017), https://www.uschamber.com/assets/archived/images/ccmc_fiduciaryrule_harms_smallbusiness.pdf (a compilation of survey statistics and other data showing that the 2016 Rule would limit or restrict investment products for some 11 million households and affect up to 7 million IRA owners, with the greatest impact on retirement savers with lower account balances) (the "Chamber Report"); Deloitte, *The DOL Fiduciary Rule: A study on how financial institutions have responded and the resulting impacts on retirement investors* (August 9, 2017), https://www.sifma.org/wp-content/uploads/2017/08/Deloitte-White-Paper-on-the-DOL-Fiduciary-Rule-August-2017.pdf (a study of institutions representing 43 percent of U.S. financial advisers and 27 percent of the retirement savings assets in the market, finding that 53 percent of firms limited or eliminated access to brokerage advice for smaller retirement accounts in response to the 2016 Rule, impacting an estimated 10.2 million accounts and $900 billion in savings) (the "Deloitte Report").

[6] Hispanic Leadership Fund, *Analysis of the Effects of the 2016 Department of Labor Fiduciary Regulation on Retirement Savings and Estimate of the Effects of Reinstatement* (November 8, 2021), https://hispanicleadershipfund.org/wp-content/uploads/2021/11/FINAL_HLF-Quantria_FiduciaryRule_08Nov21.pdf (finding that reinstatement of the 2016 Rule, or adoption of substantially similar rules, would reduce the accumulated retirement savings of 2.7 million individuals with incomes below

Proposal and our detailed comments on the Proposal in this letter are driven by a desire to avoid repeating this extremely adverse outcome for retirement savers. IRI and our members have a significant interest in this rulemaking effort, and this letter reflects our best effort to present the perspectives of those members. Unfortunately, the brief comment period provided by the Department was profoundly inadequate for stakeholders to effectively review, digest, analyze, and formulate comprehensive and substantive feedback on this extremely consequential and complex regulatory package. We will continue to engage in a robust dialogue with our members regarding the Proposal in the coming weeks, and we reserve the right to submit supplemental comments to the Department as necessary and appropriate.

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Executive Summary

1. **America's retirement income challenge and the need for retirement income products** (see pp. 6-9)
    a. Managing longevity risk is key to solving America's retirement crisis.
    b. Retirement savers need access to products that can provide a source of protected retirement income.
    c. Retirement savers who work with financial professionals are better prepared for retirement than those who do not.
    d. The Department fundamentally misunderstands annuity products.
2. **IRI's core principles for the regulation of financial professionals' conduct** (see pp. 10-14)
    a. Financial professionals should be – and already are – held to a best interest standard when recommending insurance and/or investment products to retirement savers.
    b. Retirement savers are entitled to freedom of access to retirement income protection.
    c. The availability of protected retirement income through IRA rollovers meets a critical need.
    d. Rules for annuity products must be specifically crafted to account for their protected lifetime income features.
    e. Competitive annuity markets serve the interests of retirement savers.
    f. Retirement savers have a right to choose their preferred source of retirement advice.

$100,000 by approximately $140 billion over 10 years, and would increase the wealth gap for Black and Hispanic Americans by roughly 20 percent) (the "HLF Report").

   g. Congress' public policy position in favor of access to and utilization of protected lifetime income products should be advanced.

3. **General comments on the Proposal** (see pp. 14-24)
   a. The Proposal is a solution in search of a problem.
   b. The Proposal has been inaccurately characterized as a best interest rule but would actually hold financial professionals to a far more stringent "sole interest" standard.
   c. Treating rollover and post-rollover recommendations as fiduciary investment advice under Title I of ERISA is impermissible and unnecessary.
   d. Adopting the Proposal will harm low- and middle-income retirement savers and underserved communities.
   e. The Proposal disregards the robust and effective state insurance regulatory framework and reflects a fundamental misunderstanding of annuities.
   f. The Department should deploy its limited resources to advance regulatory initiatives that will enhance retirement security.
4. **Comments on the Department's jurisdiction and legal authority to adopt the Proposal** (see pp. 24-30)
   a. The Department lacks jurisdiction to impose uniform standards for the provision of investment advice to all retirement savers.
   b. The application of the Proposal to annuities is preempted under the McCarran-Ferguson Act.
   c. The Proposal and any final rule adopted prior to Senate confirmation of a permanent Secretary of Labor may be unconstitutional and invalid.
   d. The components of the Proposal are inextricably linked and cannot be severed.
5. **Comments on the Department's rulemaking process with respect to the Proposal** (see pp. 30-32)
   a. The Department's rulemaking process with respect to the Proposal violates the letter and spirit of the Administrative Procedure Act.
   b. The Department failed to adequately consider less disruptive alternatives to the approaches taken in the Proposal.
6. **Comments on the Fiduciary Definition Proposal** (see pp. 32-38)
   a. The Fiduciary Definition Proposal fails to establish appropriate parameters for the imposition of fiduciary status under Title I of ERISA.

   b. The Fiduciary Definition Proposal would effectively prohibit many common activities that benefit retirement savers.

   c. The Fiduciary Definition Proposal includes overbroad and problematic definitions of key terms and concepts.

   d. The omission of clear and appropriate carve-outs in the Fiduciary Definition Proposal will deprive Title I Plan sponsors and participants of access to essential services and information.

7. **Comments on Both the 84-24 Proposal and the 2020-02 Proposal** (see pp. 38-45)

   a. The 84-24 Proposal and the 2020-02 Proposal are not administratively feasible.

   b. The 84-24 Proposal and the 2020-02 Proposal are not in the interests of plans and their participants and beneficiaries.

8. **Additional comments on the 84-24 Proposal** (see pp. 45-52)

   a. The strict and narrow limitations on eligibility for exemptive relief under the 84-24 Proposal are arbitrary and capricious.

   b. The 84-24 Proposal would not achieve the Department's goal of a level playing field.

   c. PTE 84-24 would no longer be administratively feasible with the overly burdensome and unworkable conditions contemplated by the 84-24 Proposal.

9. **Additional comments on the 2020-02 Proposal** (see pp. 52-53)

   a. The Department failed to appropriately consider reasonable alternatives to the approach taken in the 2020-02 Proposal.

   b. The 2020-02 Proposal would render PTE 2020-02 unworkable for insurers in the institutional market.

10. **Comments on the Other PTEs Proposal** (see pp. 53-55)

    a. The Other PTEs Proposal is impermissible under ERISA § 408(a).

    b. The Other PTEs Proposal is arbitrary and capricious.

11. **Comment on the timeline for effectiveness and implementation** (see pp. 55-56)

    a. The proposed effective date is arbitrary and capricious, and impermissible under ERISA §408(a).

12. **Comments on the Department's regulatory impact analysis** (see pp. 56-60)

    a. The Department's regulatory impact analysis relies on stale and inaccurate data.

b. The Department's regulatory impact analysis is littered with wholly unreasonable and inaccurate assumptions.

c. The Department's regulatory impact analysis ignores critical factors and information.

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<u>IRI's Comments on the Proposal</u>

I. The Context for IRI's Comments on the Proposal: America's Retirement Income Challenge and the Need for Retirement Income Products[7]

With unprecedented growth in the number of retired Americans,[8] the nation's retirement system is at a crossroads, and policymakers in Washington have taken notice. Congress enacted two comprehensive retirement bills over the past several years[9] in an effort to make protected lifetime income products more widely available. The Proposal would undermine these efforts to expand access to retirement savings, undoing advances made through bipartisan action.

A. <u>Managing longevity risk is key to solving America's retirement crisis.</u>

Americans today are at risk of outliving their assets. This longevity risk has never been greater. The rapid and continuing shift away from defined benefit plan designs in favor of a defined contribution plan model, coupled with increasing life expectancies and rising health care costs, are combining to exert significant pressures on individual retirement savers – particularly middle-income Americans – seeking a financially secure retirement. These challenges did not exist for earlier generations.

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[7] The views, concerns, and principles presented in Sections I and II of this letter are very similar to those reflected in our written comment letter on the Department's 2015 proposal titled, "Definition of the Term "Fiduciary"; Conflict of Interest Rule – Retirement Investment Advice." We reiterate these views and concerns here, updated with more recent data and information, to demonstrate that, while the regulatory framework governing the provision of advice to retirement savers has significantly evolved since 2015, the challenges facing retirement savers have, unfortunately, changed very little.

[8] *See, e.g.,* Anne Stanley, *Baby Boomers Are Hitting Peak 65. What It Means For Retirement Planning,* Investor's Business Daily (August 10, 2023), https://www.investors.com/etfs-and-funds/retirement/retirement-planning-reckoning-arrives-as-baby-boomer-generation-hits-peak-65/. ("According to the U.S. Census Bureau's population projections, about 12,000 people will turn 65 every day in the next year. That's about 4.4 million in 2024. And by 2030, all boomers — those born from 1946 through 1964 — will be 65 or older. This means one in every five Americans will have reached the traditional retirement age.").

[9] *Setting Every Community Up for Retirement Enhancement Act of 2019,* Pub.L. No. 116–94 (2019) (the "<u>SECURE Act</u>"); SECURE 2.0 Act of 2022, Division T of the Consolidated Appropriations Act, 2023, Pub. L. No. 117-328 (2022) ("<u>SECURE 2.0</u>").

At their peak in 1985, over 114,000 private-sector defined benefit plans were in place,[10] but by 2022, less than 25,000 of these defined benefit plans remained.[11] Only 15 percent of private-sector workers had access to a defined benefit plan in 2022.[12]

Individuals today are living longer than in past generations. The population of older Americans continues to increase at a faster rate than the overall population. For example, between 2010 and 2020, the 65-plus population grew by 38.6 percent, from 40.3 million to 55.8 million. This was the fastest growth rate of any decade since 1880 to 1890 (40.3 percent) and more than twice as fast as the prior decade (15.1 percent from 2000 to 2010).[13] Moreover, according to the Society of Actuaries, a married couple age 65 has more than a 65 percent chance of one or both spouses living to age 90 and a 35 percent chance of one spouse living to age 95.[14]

As a result of these trends, over 40 percent of U.S. households where the head of the household is between 35 and 64, inclusive, are projected to run short of money in retirement. Further, having adequate retirement assets is a top concern, with 44 percent of these workers believing they will not have sufficient income to last throughout retirement and will not be able to remain independent throughout retirement.[15] This reality underscores the critical importance of a regulatory environment that enables retirement savers to access products that meet their need to protect against longevity risk.

B. Retirement Savers Need Access to Products that Can Provide a Source of Protected Retirement Income.

Outside of Social Security and private pensions, annuities are the sole source of protected lifetime income during retirement. Only insurance companies and their distribution partners can provide these products. With proper planning and use, annuities provide retirees with a source of protected lifetime income and the security of knowing they will not outlive their savings.

Nine out of 10 baby boomers believe it is important for income generated from their savings to be protected for life, highlighting the importance of annuities as an integral part of retirement planning for the 85 percent of workers without access to a defined benefit plan.[16] Owning an annuity is highly correlated with confidence in retirement, as 85 percent of baby boomers who

[10] Pension Benefit Guaranty Corporation, *Trends in Defined Benefit Pension Plans.*

[11] Pension Benefit Guaranty Corporation, *Pension Benefit Guaranty Corporation Annual Report 2022.*

[12] Bureau of Labor Statistics, *National Compensation Survey: Employee Benefits in the United States, March 2022.*

[13] United State Census Bureau, *The Older Population 2020*.

[14] Society of Actuaries, *SOA 2012 Individual Annuitant Mortality tables.*

[15] Insured Retirement Institute. *Retirement Readiness Among Older Workers 2021.*

[16] *Id.*

own annuities believe their retirement savings will last until at least the age of 75, versus only 46 percent of baby boomers who do not own annuities.[17] And baby boomers who own annuities are nearly three times more likely than non-annuity owners to believe their retirement savings will last their entire lives.[18]

Annuities appeal to Americans of all income levels and retirement savers who do not have access to other retirement savings vehicles. In fact, annuity owners are overwhelmingly middle-income earners. Seven in 10 annuity owners have annual household incomes of less than $100,000. Unfortunately, as we will explain in greater detail below, the Proposal would unreasonably limit retirement savers' access to annuity products through Title I Plans[19] and individual retirement accounts ("IRAs") at precisely the point in time when access to annuities is most vitally needed.

C. Retirement Savers Who Work with Financial Professionals are Better Prepared for Retirement than Those Who Do Not.

Financial professionals play a critical role in helping retirement savers understand the wide variety of annuity products available in the market and how best to utilize them to prepare for retirement. Working with a financial professional has a positive influence on retirement planning behaviors, including increased usage of tax-advantaged savings vehicles, improved asset allocation, greater portfolio diversification, and less-speculative investing. Research shows that a financial professional can add approximately 5.12 percent to investment returns through the combination of active portfolio rebalancing, behavioral coaching, customized experience and family wealth planning, and tax-smart planning and investing.[20]

The services performed by financial professionals also translate into greater financial confidence, and greater confidence in retirement preparedness.[21] Baby boomers who work

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[17] *Id.*

[18] Insured Retirement Institute, *Boomer Expectations for Retirement 2019.*

[19] As used in this letter, the term "Title I Plans" refers to employee benefit plans described in ERISA §3(3), codified at 29 U.S.C. §1002(3).

[20] Russell Investments, *2023 Value of an Advisor* (May 9, 2023)*;* https://russellinvestments.com/Publications/US/Document/Value_of_an_Advisor_Study.pdf.

[21] *See, e.g.,* Matthew Greenwald, PhD, Greenwald Research, *The Importance of Access to Financial Guidance to Moderate Income Retirement Savers* (May 18, 2022), https://www.acli.com/-/media/acli/public/files/pdfs-public-site/public-newsroom/051822_greenwald_aclisurveymoderateincomeretirementsvrspresentation.pdf (finding that a majority of moderate-income savers who are in or near retirement are concerned that a fiduciary-only regulation would keep them from the professional financial guidance they want and need, especially during difficult economic times, with 85 percent believing they have at least a somewhat great need for financial guidance from a professional, 81 percent feeling the guidance they receive helps them feel reassured during difficult economic times, and 97 percent of savers without a financial professional believe it would be important to work with one to feel reassured through difficult economic times and during times of high inflation.)

with financial professionals are two to three times more likely to believe they are doing an effective job preparing for retirement, and that their income will last throughout retirement.[22]

It is also significant to note the particular benefits of retirement planning advice for women. Women who work with a financial professional are much more likely to be confident in their outlook on retirement. Forty percent of women who work with a financial professional say they feel very prepared for retirement, compared with 27 percent of women who do not work with a financial professional.[23] Women are also statistically more likely to live long lives, highlighting the importance of lifetime income from sources like Social Security, pensions, and annuities. In 2021, there were 89,739 centenarians in the U.S., 85 percent of whom were women.[24]

D. The Department Fundamentally Misunderstands Annuity Products.

The Proposal and related public statements by senior Department officials suggest a fundamental misunderstanding of annuity products. We have attached two IRI publications to this letter to help the Department better understand annuities and the implications of the Proposal in the annuity context.

First, IRI publishes an annual Retirement Fact Book,[25] a guide to concepts, solutions, trends, and data in the retirement income industry. The Fact Book provides detailed information on the features of annuities, illustrating the wide variety of benefits that a retirement saver could obtain from an annuity, and is known as a reliable source in the industry for annuity information and retirement topics. Chapter 4 of the Fact Book, which provides a primer on annuity products, is attached as Appendix A to this letter.

In 2023, IRI published the first edition of The IRI Retirement Saving and Income Handbook,[26] a basic guide to commonly available annuities and non-annuity alternatives. This publication provides basic information about the structure, benefits, and limitations of each solution, combined with visual representations of the mechanics of each solution and a robust glossary of key terminology. The Handbook is attached as Appendix B to this letter.

We respectfully encourage the Department to review these resources to better understand annuity products, how they work, how they are sold, and how they differ from non-insurance securities products. This information will help the Department better understand why and how the Proposal will impair the ability of retirement savers to access these valuable products.

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[22] Insured Retirement Institute, *Boomer Expectations for Retirement 2019.*

[23] LIMRA, *Impact of Financial Professionals on Retirement Security.*

[24] Boston University School of Medicine, *New England Centenarian Study.*

[25] Insured Retirement Institute, *2023 Retirement Fact Book.*

[26] Insured Retirement Institute, *Retirement Saving and Income Handbook* (2023).

II. IRI's Core Principles for the Regulation of Financial Professionals' Conduct

The following core principles have guided IRI's assessment of and comments on the Proposal:

A. Financial Professionals Should be – And Already Are – Held to a Best Interest Standard When Recommending Insurance and/or Investment Products to Retirement Savers.

IRI has long supported the application of a best interest standard to firms and financial professionals who provide advice or recommendations about insurance and/or investment products to retirement savers, and we believe the vast majority of firms and financial professionals already act in the best interest of their clients.

While the Proposal has been presented to the public as a "best interest" proposal, this is not the case. In fact, as we will discuss further below, Title I of ERISA requires fiduciaries to act "solely" in the interest of the Title I Plan and its participants.[27] As explained in the Chamber Decision, this more stringent and restrictive standard is appropriate only in circumstances involving a special relationship of trust and confidence. However, this creates a significant challenge for the Department in light of the binary nature of ERISA.

Under ERISA, firms and financial professionals are either fiduciaries whose conduct can be regulated by the Department or non-fiduciaries whose conduct falls outside the Department's jurisdiction. There is no third option. ERISA does not provide a mechanism or pathway for the Department to regulate the conduct of firms and financial professionals that have not triggered fiduciary status, nor does it allow the Department to hold such firms and financial professionals

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[27] *See, e.g.,* Bennett Aikin, *What's the difference between "sole" interests and "best" interests?* (May 13, 2015), https://www.fi360.com/blog/post/whats-the-difference-between-sole-interests-and-best-interests (outlining the differences between a "sole Interest" standard and a "best interest" standard as follows:

> "The sole interest standard is the more rigid standard, requiring that conflicts of interest in a fiduciary relationship be avoided entirely. Strictly speaking, a sole interest standard forbids even mutually beneficial transactions or compensation for the advisor. Just the opportunity for impropriety is enough to violate this standard, even if no actual harm occurs. Because of the strict interpretation of a sole interest standard, prohibited transaction exemptions are put into effect to allow for even a minimum of commerce to occur within the confines of the client-advisor relationship.
>
> "A sole interest standard exists because of the highly vulnerable position investors and beneficiaries are put into when someone else has control of their assets. It is deeply embedded in trust law, which is the foundation upon which ERISA is built.
>
> "A best interest standard is the more flexible standard. It allows for the fact that sometimes beneficiaries stand to gain the greatest benefit when the fiduciary can also benefit. The most obvious example of this is compensation. If compensation for advisors didn't exist, professional advice would not exist either and disinterested, expert advice would be exceedingly difficult to come by.
>
> "The upside of a best interest standard vs. a sole interest standard is that it incentivizes quality of services and allows for such benefits as economy of scale. The downside is that it is more open to interpretation and ripe for abuse if not carefully monitored.")

to a best interest standard rather than the more stringent "sole interest" standard once fiduciary status has been triggered.

While the Department has adopted PTE 2020-02,[28] which requires firms and financial professionals to act in their clients' best interest, the overarching "sole interest" standard still applies. Compliance with the conditions of PTE 2020-02 does not relieve a fiduciary of the "sole interest" obligation, nor is such compliance, in and of itself, sufficient to satisfy the "sole interest" standard.

Given these constraints, the Department desires to expand the reach of fiduciary status under Title I of ERISA. The Department sees this as a choice between ensuring that the conduct of financial professionals is regulated – even if such conduct would be needlessly overregulated in many instances – or allowing such conduct to be left unregulated. Fortunately, however, the broader regulatory framework governing the financial services industry is far more flexible and adaptable than ERISA.

The U.S. Securities and Exchange Commission ("SEC") and state insurance regulators operate under statutory regimes that allow for the establishment of robust best interest standards that protect retirement savers without the unnecessary and problematic restraints inherent in the "sole interest" standard imposed on ERISA fiduciaries. Historically, the SEC and state insurance regulators required financial professionals subject to their jurisdiction to satisfy a suitability standard when making individualized recommendations to their clients. In recent years, however, the overall regulatory framework governing the conduct of financial professionals has evolved. Nearly all firms and financial professionals are now held to a best interest standard by regulators with the expertise needed to craft rules that make sense for the industries to which they apply:

- The SEC adopted Regulation Best Interest ("Reg BI"),[29] which requires firms and financial professionals to act in their clients' best interest when providing advice or recommendations regarding securities.
- The National Association of Insurance Commissioners ("NAIC") adopted amendments to its model regulation on annuity sales practices (the "NAIC Model"),[30] which requires

[28] 85 FR 82798.

[29] 17 C.F.R. § 240.15l-1 (2019).

[30] *NAIC Suitability in Annuity Transactions Model Regulation (#275)* (While the official name of the NAIC Model refers to a suitability standard, the 2020 version replaced the suitability standard imposed under prior versions with a best interest standard that aligns with the standard established under Reg BI. The NAIC intentionally decided not to change the official name of the NAIC Model in order to avoid any uncertainty with respect to the requirements of §989J of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank Act"). Under §989J of the Dodd-Frank Act, certain annuities are treated as exempt from the Securities Act of 1933 if, among other things, the NAIC Model (or a successor regulation that meets or exceeds the requirements of the

firms and financial professionals to act in their clients' best interest when providing advice or recommendations regarding annuities. To date, 41 states have adopted the NAIC Model, and the remaining states are expected to do so by the end of 2024.

Collectively, these rules establish a robust framework that imposes tough but fair and workable responsibilities on the industry to effectively protect retirement savers. Further rulemaking is not needed at this time.

B. <u>Retirement Savers are Entitled to Freedom of Access to Retirement Income Protection.</u>

It is in the best interests of American workers to have the freedom to shop the financial marketplace for annuity products as a source of protected retirement income. The Proposal would severely constrain individual access to annuity products based on the assumption that individual workers are too uninformed to look out for their own interests. IRI disagrees with the premise that all retirement savers should be prejudged as incapable of looking after their own affairs and that existing regulations do not appropriately require financial professionals to act in the best interest of their clients.

C. <u>The Availability of Protected Retirement Income through IRA Rollovers Meets a Critical Need.</u>

As a result of dramatic declines in defined benefit plan coverage, coupled with the fact that very few defined contribution plans provide lifetime income forms of distribution, IRI believes individual annuity purchases through IRAs are, on a de facto basis, the primary means, other than Social Security, through which retirees procure protected retirement income. The Proposal will effectively cut off access to protected income products for most Americans when such access is most urgently needed.

D. <u>Rules for Annuity Products Must be Specifically Crafted to Account for their Protected Lifetime Income Features.</u>

Annuity products, by virtue of the protected lifetime income and other guarantees they provide, are uniquely suited to provide the financial safety and security many retirees want and need. The Proposal fails to account for the benefits and costs associated with these guarantees. In particular, the levelized distribution compensation structures that appear to be compelled by the 84-24 Proposal and the 2020-02 Proposal are incompatible with well-functioning individual annuity product distribution models and would curtail the availability of those products.

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version that was in effect when Congress enacted the Dodd-Frank Act) has been adopted by the state in which the annuity is issued or by the state of domicile of the insurance company that issues the annuity.)

E. Competitive Annuity Markets Serve the Interests of Retirement Savers.

A competitive product marketplace is in the best interests of retirement savers. Marketplace competition between and among manufacturers and other investment providers, and between and among affiliated and unaffiliated distributors, fosters innovations and efficiencies that advance the interests of retirement savers. The Proposal would stifle product innovation and price competition by superimposing a "value of services" compensation model that ignores the intrinsic value of insurance guarantees of safety and security.

F. Retirement Savers Have a Right to Choose their Preferred Source of Retirement Advice.

Retirement savers should be free from regulatory interference when selecting a financial professional. Regulators should establish appropriate guardrails to protect retirement savers against bad actors, but should not preclude retirement savers from exercising their own judgment when making such an important and highly personal decision. Some retirement savers may prefer to work with commission-based financial professionals while others may prefer the fee-based model. Some may find value in working with a financial professional who can offer products from a wide range of issuers while others may place more value on the in-depth knowledge and expertise that comes with a more limited product shelf.

The current regulatory framework effectively protects retirement savers without substituting the judgment of regulators for the preferences and priorities of retirement savers. This approach is working, as evidenced by the fact that 85 percent of baby boomers feel better prepared for retirement as a result of their financial professional's help.[31] The Proposal would deprive many retirement savers of the right to work with their preferred financial professional based on the Department's opinions about different business models and compensation practices.

G. Congress' Public Policy Position in Favor of Access to and Utilization of Protected Lifetime Income Products Should be Advanced.

IRI enthusiastically supports the recent bipartisan efforts by Congress to facilitate retirement savers' access to and use of protected lifetime income products. The SECURE Act and SECURE 2.0 included numerous provisions designed to make it easier for retirement savers to access and use annuities and other protected lifetime income products. For example, the SECURE Act established a new and improved safe harbor to guide plan fiduciaries when selecting lifetime income options for their plans,[32] a new requirement that participant benefit statements

[31] Insured Retirement Institute, *Boomer Expectations for Retirement 2018.*

[32] SECURE Act §204.

illustrate participants' total accrued benefits in the form of a "lifetime income stream,"[33] and rule changes intended to facilitate portability of lifetime income products held in plans.[34] Similarly, SECURE 2.0 updated the rules governing qualifying longevity annuity contracts ("QLACs") to enable retirement savers to allocate higher amounts to QLAC products[35] and eliminated tax penalties for partial annuitization that have served as a disincentive to the use of protected lifetime income products.[36]

These and many other changes made in these two major retirement reform statutes have been widely hailed as positive changes that will help more Americans prepare for a secure and dignified retirement. Unfortunately, the Proposal will significantly impair the value of the SECURE Act and SECURE 2.0 because, as we explain below, it will deprive countless retirement savers of access to financial professionals who can help them determine whether and how to most effectively leverage the many valuable changes made by these laws.

III. General Comments on the Proposal

Federal courts have defined "arbitrary and capricious conduct" as "willful and unreasonable action without consideration or regard for the facts and circumstances."[37] In our view, the Proposal would clearly be considered arbitrary and capricious under this standard. As explained further below, the Proposal disregards the fact that there is no evidence that existing rules are not working to effectively protect retirement savers, while also ignoring extensive evidence that the Proposal will harm many retirement savers and impose significant costs, burdens, and risks on the industry.

A. The Proposal is a Solution in Search of a Problem.

As noted above, IRI and our members have long supported efforts to ensure that financial professionals are held to a meaningful and workable best interest standard when providing personalized investment advice to retirement savers. We also recognize and appreciate the important roles played by the Department, the SEC, and state insurance regulators in ensuring that the consumers they are charged with protecting are covered by a best interest standard. This is why we supported the adoption and implementation of PTE 2020-02, Reg BI, and the NAIC Model.[38]

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[33] SECURE Act §203.

[34] SECURE Act §109.

[35] SECURE 2.0 §202.

[36] SECURE 2.0 §204.

[37] *Boothe v. Roofing Supply, Inc. Of Monroe, 893 So. 2d 123 (La. Ct. App. 2005).*

[38] IRI's expression of support for PTE 2020-02, Reg BI, and the NAIC Model should not be misunderstood as complete agreement with the entirety of each of those rules. In each case, IRI expressed concerns during the

We cannot, however, support the Proposal, which reflects the Department's continued attempts to improperly expand its jurisdiction and would make it harder for financial professionals to receive fair compensation for the hard work and effort they make to connect retirement savers with products that can help them achieve their financial goals.

PTE 2020-02, Reg BI, and the NAIC Model have been in place for a relatively brief time. The vast majority of firms and financial professionals have invested extensive time, money, and resources in good faith efforts to comply with the letter and spirit of these regulations. Using real-world experience, firms continually assess the effectiveness of their compliance efforts and refine and enhance their programs as needed. During these early stages, regulatory guidance and support can significantly enhance the ability of firms to satisfy applicable requirements and the expectations of regulators.

Similarly, pursuing enforcement actions against bad actors who intentionally violate the existing rules can provide regulators with real-world evidence as to the effectiveness of those rules. To state the obvious, the true test of the effectiveness of laws and rules is not whether they fully eliminate or prevent misdeeds by bad actors (which is impossible) but rather to ensure that regulators have the tools they need to appropriately remedy the harm suffered by victims of bad actors, to penalize bad actors, and to impair the ability of bad actors to inflict similar harm on other victims. The Proposal includes no evidence that the ability of the Department or other regulators to protect retirement savers against bad actors has been inhibited by limitations in the current regulatory framework. To the extent that regulators actually encounter such barriers to the achievement of these important goals based on gaps or flaws in their regulations, rulemaking can and should be pursued to eliminate such gaps or flaws.

In the absence of such real-world experiences, as is the case now, the continued pursuit of fundamental changes to the regulatory framework, such as those contemplated by the Proposal, is premature and less likely to result in greater protection for retirement savers. Changing the rules, yet again, will only continue to delay and interfere with the ability of the industry and regulators to effectively implement and enforce the already robust and effective best interest standards.

B. The Proposal Has Been Inaccurately Characterized as a Best Interest Rule but Would Actually Hold Financial Professionals to a Far More Stringent "Sole Interest" Standard.

In the preamble to the Fiduciary Definition Proposal, the Department notes that, "[i]nvestor confusion is exacerbated by different regulatory regimes referencing a "best interest standard"

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rulemaking process that were not fully addressed in the final rules and reserves the right to seek guidance and further rulemaking in the future to address any or all our remaining concerns.

while defining what that means and the protections that entails differently."[39] This statement, while presumably intended to support the Proposal, actually reveals one of the fundamental flaws in the Proposal – the improper and inaccurate conflation of the best interest standard established in Reg BI and the NAIC Model with the "sole interest" standard applicable to ERISA fiduciaries.

The SEC recognized that many retirement savers do not want or need the ongoing services of a fiduciary investment adviser and should not be forced to pay for such services. As a result, the SEC took great care in developing Reg BI to preserve the transactional broker-dealer business model rather than forcing all investors into the ongoing fiduciary relationship of the investment adviser business model.

The NAIC similarly opted to expressly state that the NAIC Model does not impose a fiduciary standard on insurance producers to avoid inadvertently saddling producers with ongoing monitoring obligations or other requirements that may be imposed on fiduciaries under state law.

The statutory text of ERISA, by contrast, does not impose a best interest standard, and our understanding is that a best interest standard had never been imposed under any rules or regulations promulgated by the Department prior to the 2016 Rule. Instead, under ERISA, fiduciaries are required to act "solely in the interest of [plan] participants and beneficiaries…for the exclusive purpose of…providing benefits to participants and their beneficiaries…"[40] This clearly goes far above and beyond the best interest standard established under Reg BI and the NAIC Model.

The now-vacated Best Interest Contract Exemption ("<u>BICE</u>"),[41] which was adopted by the Department as part of the 2016 Rule, incorporated the "sole interest" standard into its definition of "best interest" by requiring that recommendations be made "without regard to the financial or other interests of the Adviser, Financial Institution or any Affiliate, Related Entity, or other party."[42]

By improperly and inaccurately conflating ERISA's "sole interest" standard with the best interest standard imposed under Reg BI and the NAIC Model, the Department and supporters

[39] Fiduciary Definition Proposal, at 75921.

[40] ERISA §404(a)(1), codified at 29 U.S.C. §1104(a)(1).

[41] 81 FR 21002.

[42] *Id.*, at 21062. ("[T]he Department has retained the "without regard to" language as best capturing the exemption's intent that the Adviser's recommendations be based on the Investor's interest. This approach also accords with ERISA section 404(a)(1)'s requirement that plan fiduciaries act "solely in the interest" of plan participants and beneficiaries.").

of the Proposal have exacerbated the risk of confusion regarding the different standards that apply in different circumstances.

Department leadership and supporters of the Proposal often assert that industry objections to the Proposal are evidence of the industry's resistance to acting in the best interest of our clients, but nothing could be further from the truth. As has been stated repeatedly by IRI and many other industry organizations over the years, we are fully supportive of and committed to a best interest standard.

We cannot, however, support efforts to require all financial professionals to act in the "sole interest" of their clients. As we understand it, the "sole interest" standard requires a complete disregard of *any* financial interest of the fiduciary and its affiliates. Such a standard is incompatible with the business and economic reality that broker-dealers, registered representatives, and insurance producers only receive compensation for completed sales and rely on sales to generate enough revenue to cover their costs and earn enough to stay in business so they can support their families and continue to provide valuable services to retirement savers.

C. Treating Rollover and Post-Rollover Recommendations as Fiduciary Investment Advice Under Title I of ERISA is Impermissible and Unnecessary.

The Fiduciary Definition Proposal defines "recommendation of any securities transaction or other investment transaction or any investment strategy involving securities or other investment property" to include recommendations "as to how securities or other investment property should be invested after the securities or other investment property are rolled over, transferred, or distributed from the plan or IRA" and "[a]s to rolling over, transferring, or distributing assets from a plan or IRA, including recommendations as to whether to engage in the transaction, the amount, the form, and the destination of such a rollover, transfer, or distribution."[43] The Fiduciary Definition Proposal would treat a person who satisfies the proposed new test for fiduciary status when making a rollover or post-rollover recommendation as a fiduciary under Title I of ERISA.[44]

The attempted imposition of Title I fiduciary status in connection with rollover and post-rollover recommendations under the Proposal is further solidified by the proposed amendments to the fiduciary acknowledgment requirements in the 2020-02 Proposal and the proposed addition of corresponding fiduciary acknowledgment requirements in the 84-24 Proposal.

The Department has long argued that such regulation is necessary because "decisions to take a benefit distribution or engage in rollover transactions are among the most, if not the most,

[43] Fiduciary Definition Proposal, at 75978.
[44] *Id.*, at 75979.

important financial decisions that plan participants and beneficiaries and IRA owners and beneficiaries are called upon to make."[45] The Department further asserts that a person who recommends a rollover from a plan to purchase an annuity with the rollover proceeds would have "no obligation to adhere to a best interest standard unless they meet all prongs of the [five-part test], including regularly giving advice to the plan participant."[46]

Taken together, these statements clearly illustrate the Department's perspective that only regulation of rollover and post-rollover recommendations by the Department through the imposition of Title I fiduciary status can effectively protect retirement savers. This is factually inaccurate.

The significance of rollover and post-rollover decisions and the need for appropriate regulation of recommendations related to such decisions do not automatically confer primary responsibility for the establishment of such regulations on the Department. ERISA fiduciary status would not apply in such circumstances under the current five-part test, but Reg BI and the NAIC Model require adherence to a best interest standard in connection with rollover and post-rollover recommendations involving securities[47] and annuities, respectively.

The Department's effort to treat rollover and post-rollover recommendations as fiduciary investment advice under Title I of ERISA is incompatible with the statutory language of ERISA and the Chamber Decision. As the court explained in the Chamber Decision:

> ERISA Title II created tax-deferred personal IRAs and similar accounts within the Internal Revenue Code. 26 U.S.C. § 4975(e)(1)(B). Title II did not authorize DOL to supervise financial service providers to IRAs in parallel with its power over ERISA plans. Moreover, fiduciaries to IRAs are not, unlike ERISA plan fiduciaries, subject to statutory duties of loyalty and prudence. Instead, Title II authorized the Treasury Department, through the IRS, to impose an excise tax on "prohibited [i.e. conflicted] transactions" involving

[45] *Id.*, at 75894.

[46] *Id.*, at 75915.

[47] *Id.*, at 75897 ("The best interest standard in the SEC's Regulation Best Interest applies to broker-dealers and their associated persons when they make a recommendation to a retail customer of any "securities transaction or an investment strategy involving securities (including account recommendations).") *See also,* SEC, *Staff Bulletin: Standards of Conduct for Broker-Dealers and Investment Advisers Account Recommendations for Retail Investors*, https://www.sec.gov/tm/iabd-staff-bulletin ("When making a rollover recommendation to a retail investor, you must have a reasonable basis to believe both that the rollover itself and that the account being recommended are in the retail investor's best interest…[T]he staff believes that there are specific factors potentially relevant to rollovers that you should generally consider when making a rollover recommendation to a retail investor[, including], without limitation, costs; level of services available; features of the existing account, including costs; available investment options; ability to take penalty-free withdrawals; application of required minimum distributions; protection from creditors and legal judgments; and holdings of employer stock."); SEC, Division of Trading and Markets, *Frequently Asked Questions on Regulation Best Interest*, https://www.sec.gov/tm/faq-regulation-best-interest (last accessed on December 24, 2023).

> fiduciaries of both ERISA retirement plans and IRAs. 26 U.S.C. § 4975 (a), (b), (f)(8)(E). DOL was authorized only to grant exemptions from the prohibited transactions provision, 29 U.S.C. § 1108(a), 26 U.S.C. § 4975(c)(2), and to "define accounting, technical and trade terms" that appear in both laws, 29 U.S.C. § 1135. Title II did not create a federal right of action for IRA owners, but state law and other remedies remain available to those investors.
>
> The critical term "fiduciary" is defined alike in both Title I, 29 U.S.C. § 1002(21)(A), and Title II, 26 U.S.C. § 4975(e)(3). In Title I, fiduciaries are subject to comprehensive DOL regulation, while in Title II individual plans, they are subject to the prohibited transactions provisions.[48]

The Chamber Decision makes clear that the Department does not have the authority to establish new private rights of action – only Congress has this power. It appears, however, that the Department is seeking to circumvent this limitation by treating rollover and post-rollover advice as fiduciary investment advice under Title I of ERISA, which would make the private right of action provided in Title I of ERISA available in far broader circumstances than intended or contemplated by Congress.

Relatedly, the fiduciary acknowledgment requirement in the 84-24 Proposal and the 2020-02 Proposal, combined with the prohibition on language that would appropriately limit the scope of such fiduciary status, would force firms and financial professionals to expose themselves to private rights of action provided by a variety of existing state laws and rules. As explained in the preamble to the 2020-02 Proposal, firms and financial professionals would be required to acknowledge fiduciary status explicitly, unequivocally, and without limitation. A blanket acknowledgment of fiduciary status would likely trigger fiduciary status under state laws and rules that typically provide private rights of action to enforce the requirements of such state fiduciary laws and rules. As noted in the Chamber Decision, "whether federal or state law may be the vehicle for…lawsuits is immaterial in the absence of statutory authorization."[49]

The approach taken in the 84-24 Proposal and the 2020-02 Proposal fails to account for the fact that a firm or financial professional can be a Title I fiduciary, a Title II fiduciary, and a non-fiduciary to the same client, depending on the context in which they are interacting with the client. As a result, this would require a separate and distinct disclosure by the firm or financial professional at the outset of each interaction with the client to clearly and definitively indicate whether or not that particular interaction is covered by the Title I fiduciary standard, the Title II fiduciary standard, or neither.

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[48] Chamber Decision, at 364.

[49] Chamber Decision, at 384.

However, the Department has also made clear throughout the Proposal that disclaimers of fiduciary status are not effective. Taken together, this effectively means that a firm or financial professional that triggers Title I fiduciary status in one circumstance is automatically deemed to be a Title I fiduciary in all other cases involving the same client, as there would be no way for them to effectively limit their Title I fiduciary obligations only to those situations where they are appropriately imposed.

A series of recent District Court decisions confirmed the Department's lack of jurisdiction to extend Title I fiduciary status to rollover and post-rollover recommendations.[50]

In sum, rollover and post-rollover recommendations should be – and already are – appropriately regulated to ensure that advice about such transactions is in the best interest of retirement savers who receive such advice. Further regulation of such recommendations under ERISA as contemplated by the Proposal is both unnecessary and improper.

D. Adopting the Proposal Will Harm Low- and Middle-Income Retirement Savers and Underserved Communities.

Despite the Department's assertions to the contrary, low- and middle-income retirement savers were significantly harmed by the Department's 2016 Rule, which drove many firms and financial professionals to completely discontinue serving retirement savers with lower account balances. As outlined in great detail in the Chamber Report and the Deloitte Report, the 2016 Rule left millions of people to fend for themselves at a time when they most needed the guidance of qualified financial professionals.[51] And as explained in the HLF Report, adopting a substantially similar rule would cause a repeat of that experience, with the most severe harm likely to be experienced by Black and Latino families. [52]

While the Biden Administration has been working diligently to grow the economy from the bottom up and the middle out, a core objective of Bidenomics, the Proposal will drop the bottom out for millions of Americans who are already struggling to save for retirement by limiting their access to qualified financial professionals who can help them make informed,

[50] *See, e.g., American Securities Association v. U.S. Dep't. of Lab.*, 8:22-cv-330-VMC-CPT, at 55-57 (M.D. Fla. Feb. 13, 2023) ("ASA Decision") ("[A]ccording to the Department, the five-part test for fiduciaries applies to both Title I and the Internal Revenue Code and '[i]t would make no sense to treat someone who would satisfy the fiduciary definition with respect to the Title II plan following the rollover as exempt from fiduciary status with respect to the original rollover recommendation'.…The Court does not find this persuasive…To determine whether an individual is a fiduciary under ERISA, 'a court must ask whether a person is a fiduciary with respect to the particular activity at issue.'") (internal citations omitted). *See also, Carfora v. Teachers Insurance Annuity Association of America*, No. 1:2021cv08384 - Document 63 (S.D.N.Y. Aug. 21, 2023); and *Federation of Americans for Consumer Choice v. U.S. Dep't. of Lab.*, No. 22 Civ. 243 (K) (BT) (N.D. Tex. Jun. 30, 2023) (recommendations of Magistrate).

[51] *See* Chamber Report and Deloitte Report.

[52] *See* HLF Report.

educated decisions regarding their retirement savings. A recent study by the National Association of Insurance and Financial Advisors ("NAIFA") bears this out, finding that 72 percent of NAIFA members will have a required minimum threshold that clients must meet in order to receive financial services if the Proposal is adopted as proposed, up from 30 percent in the current regulatory environment.[53]

E. The Proposal Disregards the Robust and Effective State Insurance Regulatory Framework and Reflects a Fundamental Misunderstanding of Annuities.[54]

We strongly disagree with the Department's improper and offensive assertion that state regulation of annuity sales practices is deficient and ineffective. State regulation has been proven to work countless times over the past 150-plus years, and state regulators have the expertise and experience to assess how best to regulate annuity products and sales practices. The Department has neither.

The Proposal reflects the Department's lack of expertise and experience with respect to annuities and other insurance products. Throughout the Proposal, the Department repeatedly conflates annuities and other insurance products with mutual funds, other securities products, and other non-securities products such as real estate and commodities. This ignores the intrinsic value of insurance guarantees of safety and security, as well as the added time and work needed for a financial professional to fully understand annuity products and how they should and should not be used, and to effectively convey that information to their clients.

This inaccurate perception of annuities as equivalent – or perhaps even inferior – to securities and other investment options, as articulated in the Proposal, contributed to the development of the Proposal's unworkable approach to the regulation of annuity recommendations and sales.

This is not to suggest that the Department does not have jurisdiction over annuity recommendations made to participants in Title I Plans. The Department has important responsibilities in this regard. We merely assert that the Department can and should have confidence that state insurance regulators, who universally share the Department's commitment to robust consumer protection, have crafted a regulatory approach that is well-tailored to the unique nature of the annuity industry and appropriately balances

[53] National Association of Insurance and Financial Advisors, *Impact of the Proposed DOL Fiduciary-Only Rule on NAIFA Members* (December 2023), https://2635471.fs1.hubspotusercontent-na1.net/hubfs/2635471/NAIFA%20Members%20Respond%20to%20the%20Proposed%20US%20DOL%20Rule.pdf

[54] Consistent with the views expressed in this section, IRI supports, endorses, and agrees with the comments submitted by the NAIC to the Department regarding the Proposal. *See* NAIC letter to EBSA regarding RIN 1210–AC02 (December 21, 2023), https://content.naic.org/sites/default/files/government-affairs-rin-1210-ac02-def-fiduciary.pdf.

retirement savers' need for effective regulatory protection with their need to access products and services that help them achieve their financial objectives.

The NAIC Model provides a workable framework to regulate the conduct of insurance producers when recommending annuities, including a robust best interest standard, disclosure and conflict of interest obligations, insurer supervision requirements, and extensive producer training requirements.[55] However, the Department appears to be operating under a number of significant misconceptions about the NAIC Model:

- **Misconception #1: The NAIC Model is deficient because it expressly does not impose a fiduciary standard.** This was an intentional choice made by the NAIC to avoid inadvertently and inappropriately exposing producers to state law fiduciary standards, which would have significant risks, burdens, and implications beyond the intended purpose of the NAIC Model. Consistent with the SEC's approach in Reg BI, the NAIC opted not to shoehorn financial professionals into pre-existing fiduciary standards that are incompatible with their business models. Instead, both the NAIC and SEC focused on developing appropriate and workable rules tailored to the circumstances under which those rules would apply. By contrast, the Proposal would expose financial professionals to the risks and burdens associated with state fiduciary status under various state laws, including exposure to private litigation to enforce such laws.
- **Misconception #2: The NAIC Model fails to address conflicts of interest relating to compensation.** While cash and non-cash compensation are excluded from the definition of material conflict of interest in the NAIC Model, this was intentional to make clear that receipt of compensation is not a material conflict and that compensation conflicts for individual agents are best addressed through disclosure. Of course, the NAIC Model clearly treats certain situations as conflicts subject to the NAIC Model provisions, such as ownership interests in insurers. Given that disclosure is typically the only real-world way to mitigate compensation-related conflicts and that the NAIC Model's disclosure obligation already expressly requires meaningful compensation disclosure, the inclusion or exclusion of cash and non-cash compensation in the definition of material conflict of interest is unlikely to result in different outcomes. Moreover, consistent with Reg BI, the NAIC Model expressly prohibits sales contests and similar incentive compensation programs based on sales of particular products during specified periods of time.

[55] Laws and rules based on the NAIC Model are far from the only state insurance laws or rules that protect retirement savers. The states also have robust laws and rules that govern annuity illustrations, advertising, replacements, anti-inducement, rebating, disclosures, producer licensing, and more. The Proposal seemingly disregards the existence of these other state laws and rules entirely.

- **Misconception #3: The NAIC Model merely imposes a suitability standard, rather than a best interest standard, because the top-line best interest language is not repeated in each of the four component obligations.** In reality, the NAIC recognized that restating the best interest standard in each component would create a circular definition, where acting in your client's best interest requires compliance with component obligations that require you to act in your client's best interest. The NAIC wisely avoided this. The care obligation is designed to ensure that agents consider all their product options and recommend the one that is right for the client.

In addition to the NAIC Model, there are a myriad of state insurance laws and regulations that provide protections to retirement savers, including specific laws and regulations governing insurance advertising,[56] replacement transactions,[57] free-look periods, disclosures/buyers guides and illustrations,[58] anti-rebating/inducements/gifts,[59] and agent investigations.[60]

Congress has explicitly recognized the primacy of state insurance regulation and deferred to the expertise of state regulators on numerous occasions over the past eight decades, dating back to the passage of the McCarran-Ferguson Act ("McCarran-Ferguson")[61] in 1945. More recently, in the Dodd-Frank Act, Congress determined that fixed indexed annuities should be regulated by the states under their insurance laws and regulations, and not by the SEC as securities.[62] The Department should afford its state counterparts the same measure of respect and deference.

F. The Department Should Deploy its Limited Resources to Advance Regulatory Initiatives That Will Enhance Retirement Security.

Recent reports issued by the U.S. Government Accountability Office ("GAO")[63] and the Department's own inspector general (the "DOL IG")[64] found that EBSA has inadequate funding and staffing to support all the regulatory responsibilities assigned to it by Congress. GAO specifically noted that EBSA's "resources have generally remained unchanged while oversight responsibilities have increased over the last decade" and that EBSA "experienced a decline in staffing levels [but] has received many new responsibilities through legislation" over that same

[56] *See, e.g., NAIC Advertisements of Life Insurance and Annuities Model Regulation (#570).*

[57] *See, e.g., NAIC Life Insurance and Annuities Replacement Model Regulation (#613).*

[58] *See, e.g., NAIC Annuity Disclosure Model Regulation (#245).*

[59] *See, e.g., NAIC Unfair Trade Practices Act (#880).*

[60] *See, e.g., NAIC Producer Licensing Model Act (#218).*

[61] *McCarran-Ferguson Act*, ch. 20, 59 Stat. 33, codified as amended at 15 U.S.C. §§ 1011–1015 (1945).

[62] Dodd-Frank Act § 989J.

[63] U.S. Gov't Accountability Off., GAO-24-105667, *Employee Benefits Security Administration: Systematic Process Needed to Better Manage Priorities and Increased Responsibilities* (2023) ("GAO Report").

[64] Off. of Insp. Gen., U.S. Dep't of Labor, *Semiannual Report to Congress, Vol. 90, April 1, 2023-September 30, 2023* (2023) ("DOL IG Report").

time period.[65] Similarly, the DOL IG expressed concerns about EBSA's "ability to protect the integrity of pension, health, and other benefit plans of about 153 million workers, retirees, and their families" and its "inadequate resources to conduct compliance and enforcement." [66]

EBSA employs 752 total full-time employees, including 364 investigators to oversee roughly 747,000 employer-sponsored retirement plans, not to mention millions of group health plans and other welfare benefit plans – that's one investigator for every 2,052 retirement plans.[67] The Department now purports to have the capacity to oversee an estimated 100,000 independent producers – a figure vastly underestimated in the DOL's commentary on the Proposal.

Despite these significant challenges, EBSA has nevertheless elected to move ahead with the Proposal. Over the past thirteen years, the Department has expended substantial funds on various efforts to revise the rules defining and governing the provision of fiduciary investment advice. We respectfully suggest that the Department reevaluate its priorities and focus on enforcement of existing rules and implementation of new Congressional directives such as SECURE and SECURE 2.0 rather than continuing to divert its limited resources to this unnecessary and dangerous rulemaking project.

IV. Comments on the Department's Jurisdiction and Legal Authority to Adopt the Proposal

A. The Department Lacks Jurisdiction to Impose Uniform Standards for the Provision of Investment Advice to All Retirement Savers.

As noted above, IRI and our members fully support and agree with the premise that financial professionals should act – and should be required to act – in their clients' best interests when providing personalized advice or recommendations to retirement savers. The preamble to the Fiduciary Definition Proposal asserts that "the Department of Labor, uniquely among the regulators, can impose uniform standards for the provision of investment advice to retirement investors." [68] We strongly disagree with this assertion.

The Department clearly does not have jurisdiction to regulate the conduct of financial professionals when providing advice or other services to consumers with respect to assets held in retail accounts not covered by Title I of ERISA or §4975 of ERISA. In the context of such retail accounts, the SEC has jurisdiction over advice about securities and other securities-related services, and the state insurance departments have jurisdiction over advice about annuities and other annuity-related services. Moreover, in the Dodd-Frank Act, Congress expressly directed the SEC – and not the Department – to study and decide whether and how to pursue uniform

[65] GAO Report.

[66] DOL IG Report.

[67] GAO Report.

[68] Fiduciary Definition Proposal, at 75927.

standards of conduct for financial professionals.[69] The Dodd-Frank Act also included a provision clarifying that fixed indexed annuities are to be regulated by the states under their insurance laws and rules, and not by the SEC as securities.[70] The Chamber Decision explicitly stated that the 2016 Rule violated these provisions of Dodd-Frank:

> The Fiduciary Rule conflicts with both of these efforts. The SEC has the expertise and authority to regulate brokers and dealers uniformly. DOL has no such statutory warrant, but far from confining the Fiduciary Rule to IRA investors' transactions, DOL's regulations effect dramatic industry-wide changes because it is impractical to separate IRA transactions from non-IRA securities advice and brokerage. Rather than infringing on SEC turf, DOL ought to have deferred to Congress's very specific Dodd-Frank delegations and conferred with and supported SEC practices to assist IRA and all other individual investors. By presumptively outlawing transaction-based compensation as "conflicted," the Fiduciary Rule also undercuts the Dodd Frank provision that instructed SEC not to prohibit such standard forms of broker-dealers' compensation. And in direct conflict with Congress's approach to fixed indexed annuities, DOL's regulatory strategy not only deprives sellers of those products of the enhanced PTE 84-24 exemption but it also subjects them to the stark alternatives of using the BIC Exemption, creating entirely new compensation schemes, or withdrawing from the market. While Congress exhibited confidence in the states' insurance regulation, DOL criticizes the Dodd-Frank provisions as "insufficient" to protect the "subset" of retirement related fixed-indexed annuities transactions within DOL's purview. Certainly, however, most such products are sold to retirement investors, so DOL is occupying the Dodd-Frank turf. [71]

Despite this clear rebuke of the Department's effort to regulate fixed indexed annuities in contravention of clear and explicit Congressional action, the Proposal once again represents an improper attempt by the Department to supersede the states' laws and regulations governing annuity sales practices.

The Department does, however, have jurisdiction to administer and enforce the fiduciary, reporting, and disclosure requirements imposed under Title I of ERISA. This includes, among other things, the authority to interpret the statutory language of Title I, such as the phrase "renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so" in

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[69] Dodd-Frank Act §913.

[70] Dodd-Frank Act §989J.

[71] Chamber Decision, at 385-386. We acknowledge that the 84-24 Proposal would allow the revised exemption to be used in the context of fixed indexed annuity transactions. However, as we explain below, the 84-24 Proposal would impose unduly burdensome and unworkable conditions that would effectively require the development of "entirely new compensation schemes."

the definition of fiduciary in §3(21) of ERISA. In addition, the Department is authorized to issue exemptions from the prohibited transaction rules applicable to Title I Plans under §406 of ERISA. The Department is also responsible for enforcement of Title I and any regulations and PTEs issued thereunder.

The Department is also authorized to issue regulations, rulings, opinions, and exemptions with respect to IRAs under Title II of ERISA, which is incorporated into §4975 of the Tax Code.[72] This includes, among other things, the authority to interpret the statutory language of Title II, such as the phrase "renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so" in the definition of fiduciary in §4975(e)(3)(B) of the Tax Code. In addition, the Department is authorized to issue exemptions from the prohibited transaction rules applicable to Title I Plans under §4975(c) of the Tax Code. The Department is not responsible for enforcement of Title II of ERISA, §4975 of the Tax Code, or any regulations and PTEs issued thereunder; this enforcement authority resides with the Department of the Treasury and the Internal Revenue Service.

The Department's authority with respect to Title I Plans and IRAs is, however, constrained by the statutory text of ERISA and the Tax Code. As the Fifth Circuit Court of Appeals explained in the Chamber Decision:

> Congress chose not to require advisers to individual retirement plans to bear the duties of loyalty and prudence required of Title I ERISA plan fiduciaries. That times have changed, the financial market has become more complex, and IRA accounts have assumed enormous importance are arguments for Congress to make adjustments in the law, or for other appropriate federal or state regulators to act within their authority. A perceived "need" does not empower DOL to craft de facto statutory amendments or to act beyond its expressly defined authority.[73]

Stated more directly, the Department may not exceed its authority to impose Title I burdens and risks on firms and financial professionals operating outside of a special relationship of trust and confidence with a Title I Plan or a participant in such a plan. The Department's opinion regarding gaps in the statutory language – here, that the burdens and risks imposed on fiduciaries to Title I Plans should be extended to advice provided in other circumstances – cannot override the limitations imposed by Congress.

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[72] Presidential Reorganization Plan No. 4 of 1978, 43 FR 47713, 92 Stat. 3790, as amended Pub. L. 99–514, §2, Oct. 22, 1986, 100 Stat. 2095; Pub. L. 109–280, title I, §108(c), formerly §107(c), Aug. 17, 2006, 120 Stat. 820 , renumbered §108(c), Pub. L. 111–192, title II, §202(a), June 25, 2010, 124 Stat. 1297 ("Reorg Plan No. 4").

[73] Chamber Decision, at 379.

The Chamber Decision further established that the Department cannot override Congress' decision to preserve the "dichotomy between mere sales conduct, which does not usually create a fiduciary relationship under ERISA, and investment advice for a fee, which does."[74] ERISA fiduciary status, which requires the financial professional to act solely in the interest of the plan, participants or beneficiaries, can only be imposed where there is a special relationship of trust and confidence, which is extremely rare in the context of sales activity, even when accompanied by incidental advice.

The Department has asserted that the Fiduciary Definition Proposal is more narrowly tailored than the 2016 Rule because it would impose fiduciary status only when a retirement saver has placed their trust and confidence in a firm or financial professional. However, judicial precedent makes clear that a "special relationship of trust and confidence" requires far more than mere subjective trust by one party in another. "[N]ot every relationship involving a high degree of trust and confidence rises to the stature of a fiduciary relationship….mere subjective trust does not, as a matter of law, transform arm's-length dealing into a fiduciary relationship."[75] The Department's analysis is thus flawed as it mistakenly equates mere subjective trust with a special relationship of trust and confidence.

The Proposal clearly and blatantly disregards and is entirely inconsistent with the Chamber Decision, the common law understanding of the circumstances under which fiduciary status should properly arise, and the limitations placed on the Department's jurisdiction by Congress. As such, the Proposal must be withdrawn in its entirety.

B. The Application of the Proposal to Annuities is Preempted under the McCarran-Ferguson Act.

Congress enacted McCarran-Ferguson in 1945 in reaction to a U.S. Supreme Court ruling[76] that interpreted the Commerce Clause in the U.S. Constitution as authorizing the regulation of the insurance industry by the federal government. McCarran-Ferguson provides that "the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States." [77] This determination is reflected in the operative text of the statute, which provides that:

> "(a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

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[74] Chamber Decision, at 374.

[75] *Schlumberger Tech. Corp. v. Swanson,* 959 S.W.2d 171, 177 (Tex. 1997).

[76] *United States v. South-Eastern Underwriters Association*, 322 U.S. 533 (1944).

[77] McCarran-Ferguson, at §1011.

> (b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance…"[78]

These provisions have long been understood as prohibiting federal intrusion into the regulation of insurance except where Congress has specifically and intentionally enacted new legislation applicable to the business of insurance. While §514 of ERISA[79] does provide that ERISA supersedes state laws related to employee benefit plans, it also provides that ERISA does not "exempt or relieve any person from any law of any State which regulates insurance, banking, or securities."[80] The Proposal, to the extent applicable to annuities, would impair state laws enacted for the purpose of regulating the business of insurance and, as such, would be impermissible under the provisions of McCarran-Ferguson and §514 of ERISA.

In *Barnett Bank v. Nelson*,[81] the U.S. Supreme Court held that, under McCarran-Ferguson, a federal statute "specifically relates to the business of insurance" when it focuses directly upon industry-specific selling practices and affects the relation of insured to insurer and the spreading of risk. The Court further observed that McCarran-Ferguson "seeks to protect state regulation primarily against inadvertent federal intrusion"[82] and concluded that McCarran-Ferguson's anti-pre-emption rule would apply to "federal statutes with potentially pre-emptive effect [that] use general language that does not appear to "specifically relate" to insurance [that] conflict with state law that was enacted "for the purpose of regulating the business of insurance…"[83]

Applying the Court's reasoning to the Proposal, we note first that numerous state laws and regulations expressly permit and govern the receipt of compensation by insurance producers for their services (including but not limited to the laws and rules adopted in 41 states to date based on the NAIC Model).[84] The Proposal, if adopted as proposed, would prohibit the receipt of such compensation except if certain onerous and unworkable conditions are satisfied, thereby impairing the purposes of those state laws and rules.

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[78] *Id.*

[79] 29 U.S.C. § 1144(a).

[80] 29 U.S.C. § 1144(b)(2)(A).

[81] *Barnett Bank of Marion Cty. v. Nelson,* 517 U.S. 25 (1996).

[82] *Id.*, at 39.

[83] *Id.*, at 42.

[84] Most states have other laws and rules, beyond those that are based on the NAIC Model, that govern producer compensation. *See, e.g.,* N.Y. Ins. Law § 4228 (under which insurance companies licensed to do business in New York are permitted to employ a wide variety of compensation practices subject to specified restrictions).

We acknowledge that the savings clause in ERISA[85] could be interpreted to support the assertion that ERISA specifically relates to insurance. A compelling argument could be made, however, that ERISA applies to employee benefit plans in broad, general terms and only inadvertently applies to the business of insurance, and that the savings clause in and of itself does not definitively establish Congressional intent to directly regulate insurance under ERISA.

We also note that McCarran-Ferguson only allows Congress to enact legislation that specifically relates to the business of insurance, and that action by an executive branch agency such as the Department would not be covered by its terms. The Proposal is clearly not Congressional legislation, but we suspect the Department would assert that the Proposal is merely an interpretation of legislation that is not preempted by McCarran-Ferguson, and therefore should enjoy the same insulation from preemption. This position should not prevail, given that the Proposal is focused primarily on one discrete provision of ERISA that imposes fiduciary status on providers of "investment advice."

Congress could have easily referred to "investment and/or insurance advice" in §3(21) of ERISA, but it chose instead to refer only to "investment advice." McCarran-Ferguson explicitly states, "silence on the part of the Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States."[86] Given Congress' silence as to the inclusion of insurance in the phrase "investment advice," McCarran-Ferguson could be applied to prohibit the Department from interpreting "investment advice" in a manner that encompasses advice about insurance products.

C. The Proposal and Any Final Rule Adopted Prior to Senate Confirmation of a Permanent Secretary of Labor May Be Unconstitutional and Invalid.

Acting Secretary of Labor Julie Su has served in that role since March 11, 2023, and her formal nomination to serve as the permanent Secretary of Labor was transmitted to Congress just three days later. We understand that the Biden Administration has taken the position that, while Acting Secretary Su lacks adequate support to secure Senate confirmation, she may and will continue to serve in an acting capacity indefinitely based on the administration's interpretation of the Federal Vacancies Reform Act[87] and the Labor Code.[88] A detailed analysis of the validity of actions taken by the Department under these circumstances is beyond the scope of this letter. That being said, we believe there are strong, compelling, and legally sound arguments that any actions taken by the Department in this regard under the leadership of an

[85] 29 U.S.C. §1144(b)(2)(A).
[86] McCarran-Ferguson, at §1011.
[87] 5 U.S.C. § 3341 et seq.
[88] 29 U.S.C. §552.

Acting Secretary under the present circumstances would violate Article II, Section 2 (the Appointments Clause) of the U.S. Constitution[89] and would therefore be invalid.

D. The Components of the Proposal are Inextricably Linked and Cannot be Severed.

The Proposal notes that the Department "generally intends discrete aspects of this regulatory package to be severable [such that] the updated regulatory definition of a fiduciary would survive even if a court vacated any of the amendments to the PTEs leaving in place the previously granted versions of those PTEs."[90] We disagree with this assessment. The proposed changes to the rules that determine when investment advice fiduciary status is triggered and proposed changes to the rules that govern the ability of investment advice fiduciaries to receive reasonable compensation for their services are so inextricably linked that neither should be able to survive in the absence of the other. Just as the Fifth Circuit ruled in the Chamber Decision in 2018, "this comprehensive regulatory package is plainly not amenable to severance."[91]

V. Comments on the Department's Rulemaking Process with Respect to the Proposal

A. The Department's Rulemaking Process with Respect to the Proposal Violates the Letter and Spirit of the Administrative Procedure Act.

The Department provided just 60 calendar days for stakeholders to submit comments on the Proposal. This translated into just 39 business days when accounting for the several major federal, religious, and cultural holidays that fell within the comment period. Such a short comment period for major federal rulemaking affecting retirement planning and financial security for millions of workers and retirees does not allow for meaningful public engagement and is inconsistent with the Department's past practice of providing at least 75 to 105 days for interested stakeholders to comment on prior iterations of the Proposal. The Department nevertheless rejected a reasonable request to extend the comment period time.

In addition, the Department scheduled and held a public hearing on December 12th and 13th, 2023, before the end of the comment period and a week earlier than initially indicated in its announcement of the Proposal. Public hearings are typically held after an agency receives comments, with additional time for stakeholders to supplement their written comments after the hearing. In this case, however, the Department arbitrarily and needlessly elected to deviate from its past practice to unreasonably accelerate the rulemaking process, creating the

[89] U.S. Const. art. II, §2.

[90] Fiduciary Definition Proposal, at 75912.

[91] Chamber Decision, at 388.

appearance that the Department is unlikely to make meaningful changes to the Proposal based on public comments.[92]

Moreover, the preambles to each component of the Proposal collectively seek public input on well over a hundred important (and in many cases, fundamental) questions and topics that should have been addressed before the Department undertook formal rulemaking. For example, the preamble notes that "the Department intends to examine the ways investment advice providers market themselves and describe their services."[93] The Department should have sought stakeholder input on these types of questions through a request for information rather than moving directly to issuance of the Proposal.

B. <u>The Department Failed to Adequately Consider Less Disruptive Alternatives to the Approaches Taken in the Proposal.</u>

Federal regulatory agencies are generally required to identify and consider reasonable alternatives that could achieve the desired outcome in a more efficient or less disruptive manner.[94] In our view, the Department has not satisfied this obligation.

For example, the Department has asserted, in part, that the Fiduciary Definition Proposal is necessary because the five-part test enables firms and financial professionals to avoid fiduciary status by including a disclaimer of fiduciary status in fine print disclosures. However, the five-part test is already a functional test, meaning that courts should not give effect to any attempted disclaimer of fiduciary status if the conduct of the parties makes clear that a fiduciary relationship exists. Moreover, even if this were not the case, the Department should have considered whether this theoretical concern could have been addressed in a less disruptive manner, such as a requirement that any purported disclaimer of fiduciary status

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[92] Public comments by senior Department officials – and even President Biden's comments at the press release during which the Proposal was announced – can be interpreted to suggest that the Department has already decided how to proceed, such that the notice-and-comment period is nothing more than a check-the-box exercise. For example, President Biden stated, "[i]f this rule is finalized as proposed, it's going to protect workers and it's going to save for —that are saving for their retirements." Moreover, in her letter rejecting the industry's reasonable request that the comment period be extended and that the public hearing be delayed, Assistant Secretary Lisa Gomez stated, "EBSA believes that its current proposal reflects significant input it has received from public engagement with this project since 2010, and…has engaged informally with numerous stakeholders representing multiple viewpoints on issues related to the proposed rulemaking package. Therefore, at this point, EBSA does not intend to extend the comment period or delay the hearing." Judicial precedent makes clear that an illusory notice-and-comment period does not satisfy the requirements of the Administrative Procedure Act. *See, e.g., Nehemiah Corp. of America v. Jackson*, 546 F. Supp. 2d 830 (E.D. Cal. 2008) (holding that "[a]llowing the public to submit comments to an agency that has already made its decision is no different from prohibiting comments altogether. Indeed, if the public perceives that the agency will disregard its comments, there may be a chilling effect that causes the public to refrain from submitting comments as an initial matter.")

[93] Fiduciary Definition Proposal, at 75903.

[94] *See, e.g.,* Exec. Order No. 12866, *Regulatory Planning and Review*, 58 FR 51735 (October 4, 1993).

would be effective only if presented in an adequately prominent fashion and/or if the financial professional has a reasonable basis to believe that the client understands and agrees to such a disclaimer. Nothing in the Fiduciary Definition Proposal suggests that the Department considered this reasonable and less disruptive alternative approach.

Throughout this letter, we will identify a number of other aspects of the Proposal where the Department seemingly failed to satisfy its obligation to consider reasonable alternatives.

VI. Comments on the Fiduciary Definition Proposal

A. The Fiduciary Definition Proposal Fails to Establish Appropriate Parameters for the Imposition of Fiduciary Status Under Title I of ERISA.

Under current rules, a person is a fiduciary only if they: (1) render advice as to the value of securities or other property, or make recommendations as to the advisability of investing in, purchasing, or selling securities or other property (2) on a regular basis (3) pursuant to a mutual agreement, arrangement, or understanding with the plan or a plan fiduciary that (4) the advice will serve as a primary basis for investment decisions with respect to plan assets, and that (5) the advice will be individualized based on the particular needs of the plan.[95]

In the Chamber Decision, the Fifth Circuit stated that this five-part test "captured the essence of a fiduciary relationship known to the common law as a special relationship of trust and confidence between the fiduciary and his client."[96] We agree with this assessment. In particular, the regular basis, mutual understanding, and primary basis prongs of the five-part test – which would be eliminated under the Fiduciary Definition Proposal – reflect the fact that a special relationship of trust and confidence cannot spring into existence spontaneously but rather must be intentionally cultivated over time.

The Department, however, has asserted that this test is "underinclusive because it fails to capture many circumstances in which an investor would reasonably believe they were receiving advice from an investment professional who was rendering services to the investor based upon the investor's best interest."[97]

The Fiduciary Definition Proposal would replace this five-part test with a new test under which a firm or financial professional will be a fiduciary under ERISA when recommending an investment transaction to a Title I Plan or a fiduciary, participant, or beneficiary of a Title I Plan, or to an IRA or an owner, fiduciary, or beneficiary of an IRA, if the firm or financial professional makes recommendations to retirement savers on a regular basis as part of their business and

[95] 29 CFR 2510.3–21(c)(1).

[96] Chamber Decision, at 365.

[97] Fiduciary Definition Proposal, at 75899.

the circumstances indicate that the recommendation is based on the retirement saver's particular needs or situation and can be relied upon by the retirement saver as being in their best interest.

While the reasonable expectations of retirement savers should be taken into account when determining when fiduciary status should arise, other factors are also relevant and must be considered. The five-part test recognizes these other factors whereas the Fiduciary Definition Proposal disregards them and focuses solely on retirement savers' expectations (and, arguably, the Department's opinion as to whether a relationship of trust and confidence should exist in any particular circumstance).

Trust and confidence must be earned; they are not commodities that can be bought and sold. By removing the regular basis prong in the five-part test, the Fiduciary Definition Proposal reflects a failure to understand this basic fact.

Moreover, a special relationship of trust and confidence is, by definition, tied to the particular individuals involved in that relationship. Whether a financial professional makes recommendations to other retirement savers on a regular basis as part of their business has no bearing on the nature of the financial professional's relationship with any particular client.

Lastly, conditioning fiduciary status on whether a recommendation "can be relied upon by the retirement saver as being in their best interest"[98] serves no meaningful purpose in the current insurance regulatory environment. All financial professionals in the insurance industry are now required to act in their clients' best interest, whether under PTE 2020-02, Reg BI, or state insurance laws and rules based on the NAIC Model.

B. The Fiduciary Definition Proposal Would Effectively Prohibit Many Common Activities That Benefit Retirement Savers.

The Fiduciary Definition Proposal inappropriately characterizes as fiduciary in nature a broad spectrum of financial marketing and sales activities where no reasonable expectation can exist that the retirement saver has engaged the firm or financial professional to act as an unbiased and impartial source of recommendations under a legal obligation to disregard its own interests as a seller of financial products and services. Firms and financial professionals should be permitted to recommend products they believe are in a retirement saver's best interest without necessarily triggering fiduciary status under Title I of ERISA by making such a recommendation. The Fiduciary Definition Proposal would make this impossible.

Firms and financial professionals engage in a wide range of activities that have significant value to retirement savers but should not be considered "advice" that would give rise to fiduciary

[98] Fiduciary Definition Proposal, at 75977.

status within the ambit of this rulemaking. Listed below are just a few examples of such activities. However, despite assertions to the contrary by the Department, each of these activities would seemingly be captured under the Fiduciary Definition Proposal and would likely have to be discontinued if the Proposal is adopted:

- Call center representatives and other administrative staff providing sales, marketing, informational, or educational materials or answering general questions and providing general customer services;
- Giving a mere factual description of the features of an annuity product, such as an immediate fixed annuity or a deferred variable annuity, and explaining how the product can meet certain needs;
- Responding to a request for proposal or other inquiry by submitting a description of a product that may fit the needs of a plan, including a sample fund line-up;
- Offering, marketing, or otherwise making available a plan recordkeeping service which includes access to a platform of available investment options that a retirement plan sponsor may select from to serve as its plan investment option menu;
- “Hire me” activities involving the offering of advisory service capabilities, including past performance and available investment strategies;
- Provision of recommendations to a plan or retirement saver by a person who is affiliated with a firm that provides discretionary asset management services to the plan or retirement saver;
- Routine participant plan enrollment activities, including education and recommendations to enroll in the plan;
- Answering questions from plan participants about the operation of an “in-plan” protected lifetime income product and its available features;
- Proprietary product “wholesaling” activities where representatives of an annuity product provider meet with financial professionals – either one-on-one or in group sessions – to explain the features of the product and to conduct training;
- Providing a brochure to a prospective purchaser describing the features of one or more annuity products available for sale through a registered broker-dealer;
- Presenting to a prospective annuity purchaser a list of investments that are available under a variable annuity product;

- Explaining basic asset allocation concepts and providing examples of how one or more particular annuity products could be used to implement an individual's asset allocation plan;
- Counseling a recent retiree about their likely income replacement needs and the features available under various annuity products that could help meet those income replacement needs; and
- Referral of a client by one financial professional to another who specializes in annuity products and has specialized knowledge and training in annuity features.

C. The Fiduciary Definition Proposal Includes Overbroad and Problematic Definitions of Key Terms and Concepts.

The definitions and interpretations of several key terms and concepts in the Fiduciary Definition Proposal are significantly and inappropriately overbroad and incompatible with ERISA and judicial precedent.

1. Overly Broad Definition of "Recommendation"

The Fiduciary Definition Proposal defines "recommendation of any securities transaction or other investment transaction or any investment strategy involving securities or other investment property" to mean recommendations:

> (i) As to the advisability of acquiring, holding, disposing of, or exchanging, securities or other investment property, as to investment strategy, or as to how securities or other investment property should be invested after the securities or other investment property are rolled over, transferred, or distributed from the plan or IRA;
>
> (ii) As to the management of securities or other investment property, including, among other things, recommendations on investment policies or strategies, portfolio composition, selection of other persons to provide investment advice or investment management services, selection of investment account arrangements (e.g., account types such as brokerage versus advisory) or voting of proxies appurtenant to securities; and
>
> (iii) As to rolling over, transferring, or distributing assets from a plan or IRA, including recommendations as to whether to engage in the transaction, the amount, the form, and the destination of such a rollover, transfer, or distribution.[99]

While the Department asserts that this definition aligns with the SEC's definition and interpretation of "recommendation" in Reg BI, it differs in important and meaningful ways.

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[99] Fiduciary Definition Proposal, at 75978-75979.

Most notably, in the preamble to the Fiduciary Definition Proposal, the Department clarifies its intent, noting that, "[f]or purposes of the proposed rule, the Department views a recommendation as a communication that, based on its content, context, and presentation, would reasonably be viewed as a suggestion that the retirement investor engage in or refrain from taking a particular course of action."[100] The SEC has clearly explained on numerous occasions that a "recommendation" exists only where there is "a call to action." A mere suggestion would fall far short of "a call to action" and thus would not be treated as a recommendation under Reg BI, but seemingly would suffice under the Fiduciary Definition Proposal.

The Department further notes that "the fact that a communication is made to a group rather than an individual would not be dispositive of whether a recommendation exists"[101] and "providing a selective list of securities to a particular retirement investor as appropriate for the investor would be a recommendation as to the advisability of acquiring securities even if no recommendation is made with respect to any one security." [102] Under Reg BI, neither of these examples would be considered calls to action, and therefore, neither would constitute recommendations.

2. *Overly Broad Definition of "Retirement Investor"*

The term "Retirement Investor" is not included in the "Definitions" section of the Fiduciary Definition Proposal but appears to be defined in the operative text to include plans, plan fiduciaries, plan participants and beneficiaries, IRAs, IRA owners and beneficiaries, and IRA fiduciaries. It is inappropriate and unnecessary for advice to plans and their fiduciaries to be subjected to the same rules that govern advice provided to individual retirement savers.

While it is true that neither Reg BI nor the NAIC Model covers advice to plans or plan sponsors, the Department has provided no evidence that plans, plan sponsors, or IRA fiduciaries are actually being harmed by conflicted advice and that the Department does not have the tools it needs under current rules to protect plans, plan sponsors, or IRA fiduciaries against such harm. If the Department has real-world evidence of such harm, it should seek public input to guide a targeted rulemaking project to address that particular issue. Lumping plans, plan sponsors, and IRA fiduciaries into a rulemaking effort focused on advice provided to individual retirement savers ignores the extensive and important differences between individuals and institutional entities.

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[100] *Id.*, at 75904.

[101] *Id.*

[102] *Id.*

In addition, the term “Retirement Investor” is included in the ‘Definitions’ sections of the 2020-02 Proposal and the 84-24 Proposal, and in both cases, the term is defined far more narrowly, including only plan participants and beneficiaries, IRA owners, and fiduciaries to plans and IRAs. The Department has provided no explanation for the different meanings ascribed to this term.

3. Overly Broad Definition of “For a Fee or Other Compensation, Direct or Indirect”

The interpretation of “for a fee or other compensation, direct or indirect” as encompassing a broad array of compensation incident to the transaction is inconsistent with ERISA and the Chamber Decision. As the Court noted, the federal securities laws have long recognized that firms and financial professionals receive no compensation for the provision of advice that is incidental to brokerage services, and therefore, such incidental advice is not sufficient to trigger fiduciary status under the Advisers Act.[103]

Congress was well aware of the securities law approach and could have expressly stated in ERISA that compensation paid for brokerage services would be attributed also to any incidental advice provided in connection with such services, such that incidental advice would be sufficient to trigger ERISA fiduciary status. Under the rules of statutory construction, the absence of such express language in ERISA means that Congress chose not to override the securities law approach. The Department may disagree with this approach, but only Congress has the authority to change it.

D. <u>The Omission of Clear and Appropriate Carve-Outs in the Fiduciary Definition Proposal Will Deprive Title I Plan Sponsors and Participants of Access to Essential Services and Information.</u>

The Fiduciary Definition Proposal lacks appropriate and effective carve-outs for conduct that should not be treated as fiduciary. In contrast, the 2016 Rule included carve-outs and exceptions from the definition of recommendation for (i) platform providers, (ii) selection and monitoring assistance, (iii) general communications, and (iv) investment education (including plan information; general financial, investment, and retirement information; asset allocation models; and interactive investment materials). The 2016 Rule also included exceptions from fiduciary status for (1) transactions with independent fiduciaries with financial expertise; (2) swap and security-based swap transactions; (3) and the conduct of employees of plans, plan sponsors or affiliates, or plan fiduciaries.

The Department asserts in the preamble that such carve-outs are not needed in the Fiduciary Definition Proposal because the facts and circumstances covered by these carve-outs would not trigger fiduciary status under the proposed new test.[104] While we appreciate this general

[103] Chamber Decision, at 372-373.
[104] *Id.*, at 75907-75909.

statement of the Department's intent, we do not believe it is sufficient or appropriate to expect the industry to rely on informal guidance on such a fundamental aspect of the Fiduciary Definition Proposal.

Moreover, we are extremely concerned that conversations between financial services firms (including but not limited to their consultants, wholesalers, and salespeople) and plan sponsors (or with other financial professionals acting as fiduciaries to plans and IRA owners) would likely trigger fiduciary status under the Proposal. Imposing fiduciary status in such circumstances will adversely impact the provision of information to plans or plan fiduciaries in the institutional space, such as in the case of wholesaler relationships, pension risk transfer transactions, and sales of QLACs and stable value funds to Title I Plans and health savings accounts.

VII. Comments on Both the 84-24 Proposal and the 2020-02 Proposal[105]

The 84-24 Proposal and the 2020-02 Proposal include many identical (or nearly identical) provisions. This section outlines our concerns about these provisions. In the sections that follow, we will discuss additional concerns we have with respect to provisions in the 2020-02 Proposal that are not identical to the 84-24 Proposal and with respect to provisions in the 84-24 Proposal that are not identical to the 2020-02 Proposal.

A. The 84-24 Proposal and the 2020-02 Proposal Are Not Administratively Feasible.

ERISA §408(a) authorizes the Department to grant PTEs from the restrictions of ERISA sections 406 and 407(a) for fiduciaries to Title I Plans in instances where the Secretary makes a finding on the record that relief is (1) administratively feasible, (2) in the interests of the Title I Plan and its participants and beneficiaries, and (3) protective of the rights of participants and beneficiaries of such Title I Plan. Tax Code §4975(c)(2) establishes identical requirements for the issuance of PTEs from Tax Code §4975(c)(1).[106] Given the complexities of the 84-24 Proposal and the 2020-02 Proposal, and for the specific reasons noted below, we do not believe it would be administratively feasible for the industry to implement the proposed changes to PTE 84-24 and PTE 2020-02 or for the Department to effectively and consistently oversee and enforce compliance with those changes.

[105] As used throughout Sections VII and VIII of this letter in relation to the 84-24 Proposal, the terms Insurer, Independent Producer, and Insurance Sales Commission have the meanings ascribed to such terms in the 84-24 Proposal.

[106] Reorg Plan No. 4 (transferring authority to issue exemptions from Tax Code §4975(c)(1) from the Secretary of the Treasury to the Secretary of Labor.)

1. *Administratively Unfeasible Regulation of Conflicts Arising from Unconscious Interests*

The 84-24 Proposal defines "conflict of interest" as "an interest that might incline a Financial Institution or Investment Professional—consciously or unconsciously—to make a recommendation that is not in the Best Interest of the Retirement Investor."[107] The 2020-02 Proposal similarly defines "conflict of interest" as "an interest that might incline a Financial Institution or Investment Professional—consciously or unconsciously—to make a recommendation that is not in the Best Interest of the Retirement Investor."[108] However, the Department offers no insight as to how a firm or financial professional can identify, manage, or mitigate unconscious factors, nor does the Department explain how an unconscious factor could negatively impact investment advice. Unless and until the ability to read minds moves out of the realm of science fiction and into reality, it will be administratively and practically unfeasible for the industry to comply with this requirement and for the Department to effectively monitor compliance and determine when to pursue enforcement.[109]

2. *Administratively Unfeasible Requirement that Disclosures Reflect Level of Financial Experience*

The preambles to the 84-24 Proposal and the 2020-02 Proposal indicate that disclosures must be presented in plain English, "taking into consideration a Retirement Investor's level of financial experience." All retirement savers have different levels of financial literacy and sophistication, though, so the disclosures would effectively have to be individualized to more than 100 million unique retirement savers to satisfy this requirement.

For the industry, it would be nearly impossible to develop and implement policies and procedures that could both allow for the development of such individualized disclosures and ensure that such disclosures fully comply with all applicable legal requirements. Even for the small fraction of the industry that could potentially do so, the process would be extraordinarily expensive and time-consuming.

[107] 84-24 Proposal, at 76031.
[108] 2020-02 Proposal, at 76002-76003.
[109] We acknowledge that the SEC, in Reg BI, defines "conflict of interest" to include conflicts arising from unconscious interests on nearly the same terms as reflected in the 84-24 Proposal and the 2020-02 Proposal. We expressed similar concerns in our written comments to the SEC on the proposal to establish Reg BI. We disagreed with the SEC's decision to retain that language in the final version of Reg BI, and we remain concerned about the implications of that decision. While alignment across regulatory jurisdictions is typically appropriate and beneficial, in this case, such alignment would serve to exacerbate our concerns.

For the Department, there would be no feasible way to effectively monitor the sheer volume of disclosures that would be impacted to appropriately and consistently enforce this requirement.

3. *Administratively Unfeasible Requirement that Disclosures be Presented in Actual Dollars*

Disclosures about fees and costs cannot always be provided in actual dollars, as compensation structures are often tied to the value of assets at particular times and can therefore fluctuate. The 84-24 Proposal and the 2020-02 Proposal fail to recognize this fact, which would make it administratively and practically unfeasible for the industry to comply with this requirement.

4. *Administratively Unfeasible Treatment of Omissions as Misleading Statements*

Both the 84-24 Proposal and the 2020-02 Proposal specify that the prohibition on misleading statements as part of the Impartial Conduct Standards would also prohibit "omitting information that is needed to prevent the statement from being misleading to the Retirement Investor under the circumstances." [110] This would be administratively unfeasible in the absence of appropriate and workable qualifications, such as a requirement that the omission was intentional or negligent, or even a requirement that the person making the statement had actual knowledge of allegedly omitted information.

5. *Solicitation of Feedback on Administratively Unfeasible Public Website Disclosure Requirement*

Both the 84-24 Proposal and the 2020-02 Proposal specifically request feedback from stakeholders as to whether the exemptions should be further revised to require disclosure of certain information on a publicly available website, including pre-transaction disclosures, descriptions of a firm's or financial professional's business model, associated conflicts of interest (including arrangements that provide third party payments), and a schedule of typical fees. IRI and our members would strongly oppose any such requirement. Establishing and maintaining such websites would require significant time, money, and resources. Clients and prospective clients have access to a wide range of information upon request at any time. We do not see the need to require a publicly available website, especially in light of the costs involved.

[110] 84-24 Proposal, at 76027; 2020-02 Proposal, at 76000.

B. The 84-24 Proposal and the 2020-02 Proposal Are Not in the Interests of Plans and Their Participants and Beneficiaries.

1. Conflation of Impartial Conduct Standards and "Sole Interest" Standard

As explained above, the 84-24 Proposal and the 2020-02 Proposal improperly conflate the impartial conduct standards with the "sole interest" standard to which fiduciaries are held under Title I of ERISA. See Section III.A. of this letter for our detailed explanation as to why and how this would harm plans, participants, and beneficiaries. Imposing fiduciary status under Title I of ERISA on all firms and financial professionals rather than limiting such status to only those circumstances in which there is a true relationship of trust and confidence will deprive millions of retirement savers of the ability to obtain advice that is in their best interest from their preferred firm and/or financial professional.

The very concept of imposing fiduciary status on all financial professionals on a transaction-by-transaction and exemption-by-exemption basis is fundamentally flawed and inconsistent with federal securities law and state insurance regulation. As we note above, the SEC was careful to preserve the distinction between a registered representative's transactional best interest obligations and the ongoing fiduciary obligations owed by investment adviser representatives. The Proposal rejects this sensible and appropriate distinction in a misguided and dangerous effort to establish one rule to govern all relationships and activities.

2. Overly Broad and Restrictive Prohibition on Incentive Compensation Programs

The 84-24 Proposal and the 2020-02 Proposal would prohibit the use of "quotas, appraisals, performance or personnel actions, bonuses, contests, special awards, differential compensation, or other similar actions or incentives that are intended, or that a reasonable person would conclude are likely, to result in recommendations that are not in Retirement Investors' Best Interest." [111] In addition, the preambles to both the 84-24 Proposal and the 2020-02 Proposal assert that "[a] Financial Institution should not offer incentive vacations, or even paid trips to educational conferences, if the desirability of the destination is based on sales volume and satisfaction of sales quotas." [112]

This would operate, in effect, as an almost complete prohibition on the use of incentive compensation. This departs significantly from the approach taken in the original version of PTE 2020-02. The Department provides no clear rationale for such an abrupt change so soon after publishing the original exemption.

[111] 84-24 Proposal, at 76028; 2020-02 Proposal, at 76001.
[112] 84-24 Proposal, at 76011; 2020-02 Proposal, at 75987.

Importantly, this provision is also substantially more restrictive than the approach taken by the SEC and state insurance departments. Under Reg BI and the NAIC Model, incentive compensation is only prohibited outright when tied to sales of particular products within a limited period of time, and other applicable state laws and regulations expressly authorize and regulate other forms of compensation.[113]

To be clear, we are not suggesting that incentive compensation programs should be free from regulatory oversight or that such programs should be universally permitted. Instead, our objection to this provision is that the Department's approach ignores important and meaningful distinctions and nuances that necessitate more thoughtful and careful rulemaking that is incompatible with the one-size-fits-all regulatory framework reflected in the Proposal.

Compensation practices can be designed and used for a wide range of purposes. For example, compensation practices can be used to encourage financial professionals to re-evaluate their preconceived notions about products that meet particular financial needs or goals or to offset the added work required to sell certain types of products. Broadly prohibiting incentive compensation programs would result in many retirement savers losing access to products that could be in their best interest. Clearly, this would not be in the interest of plans, participants, and beneficiaries.

3. Draconian Eligibility Provisions

The 84-24 Proposal and the 2020-02 Proposal include provisions that would force entire enterprises out of the retirement business for ten years due to convictions of affiliates or even family members of affiliates for a wide range of offenses, whether in the U.S. or in foreign countries, even for convictions that are unrelated to the provision of investment advice or other services to American retirement savers. These disqualification provisions are draconian and not in the interests of plans and their participants and beneficiaries.

Under these provisions, a fiduciary investment advice provider would lose eligibility to use PTE 84-24 and PTE 2020-02 even if, for example:

- the misconduct forming the basis for the conviction occurred prior to the effective date contemplated by the Proposal;
- the misconduct forming the basis for the conviction is entirely unrelated to the provision of services to retirement plans or retirement savers;
- the convicted individual never colluded with any individuals involved in the provision of services to retirement plans or retirement savers;

[113] See, e.g., N.Y. Ins. Law § 4228 (under which insurance companies licensed to do business in New York are permitted to employ a wide variety of compensation practices subject to specified restrictions).

- neither the fiduciary investment advice provider nor its directors, officers, or employees participated in the misconduct; or
- no plans or plan assets were involved or affected by the misconduct forming the basis for the conviction.

Even the most robust and effective compliance programs cannot fully prevent criminal conduct by affiliates or their family members. This is particularly troubling given that the criminal justice systems in many foreign nations do not provide the same due process protections we enjoy in this country. This is also unnecessary, as Congress has already enacted a crime bill that establishes appropriate penalties for crimes related to the business of insurance.[114] Moreover, most states require that an insurance producer be competent, trustworthy, and of good moral character in order to obtain an insurance license. Such agent investigations are undertaken either by the state insurance regulator or by the insurer prior to requesting the producer be appointed as its agent.

Neither the 84-24 Proposal nor the 2020-02 Proposal provide meaningful arguments to support the imposition of such extreme consequences, nor do they offer any insights or guidance as to how a firm or financial professional could protect itself against the risk of such consequences.

This unworkable and inequitable approach to disqualification will harm plans and participants, who would face significant negative consequences and costs if their fiduciary investment advice provider loses eligibility to rely on PTE 84-24 and PTE 2020-02. A disqualified provider would only be permitted to provide services that do not require exemptive relief to avoid violating the prohibited transaction rules. As a result, most plans and participants would need to transition to a new provider, which will result in significant transition costs and burdens, such as the costs and time required for a Request for Proposal process, costs associated with consultants to assist or manage the process, legal review and negotiation of new agreements, and other due diligence expenses.

Due to the draconian, self-effectuating disqualification provisions in the 84-24 Proposal and the 2020-02 Proposal, and the wholly inadequate "opportunity to be heard" provision, plans and their participants and beneficiaries would face a perpetual risk of losing access to their selected advice provider based on entirely unrelated and irrelevant circumstances, with no way to effectively manage or mitigate this risk. This would not be in the interests of the plan and its participants and beneficiaries.

[114] 18 U.S.C. § 1033.

4. Overly Broad Access to Records

The 84-24 Proposal would require the maintenance of

> …records necessary to…determine whether the conditions of this exemption have been met with respect to a transaction for a period of six years from the date of the transaction in a manner that is reasonably accessible for examination…[which must be made] reasonably available at their customary location during normal business hours for examination by: (A) Any authorized employee of the Department or the Internal Revenue Service or another state or federal regulator; (B) Any fiduciary of a Plan that engaged in a transaction pursuant to this exemption; (C) Any contributing employer and any employee organization whose members are covered by a Plan that engaged in a transaction pursuant to this exemption; or (D) Any participant or beneficiary of a Plan or beneficial owner of an IRA acting on behalf of the IRA that engaged in a transaction pursuant to this exemption."[115]

The 2020-02 Proposal seeks public input as to whether the recordkeeping provision of PTE 2020-02 should be amended to align with this provision. We oppose the inclusion of this provision in both exemptions.

We acknowledge that the 84-24 Proposal further clarifies that "[n]one of the persons described in subsection (2)(B)–(D) above are authorized to examine records regarding a transaction involving another Retirement Investor, privileged trade secrets or privileged commercial or financial information of the Insurer, or information identifying other individuals."[116] The request for feedback on this subject in the 2020-02 Proposal contemplates the inclusion of the same limitations.

To be clear, our objection is not to the inclusion of recordkeeping provisions but to the needlessly and inappropriately broad universe of persons to whom access must be provided. Clearly, the Department would need access to such information to effectively enforce the requirements of the applicable exemption. However, the Department provides no explanation as to why such sensitive information needs to be made so widely available.

In our view, allowing plan fiduciaries and employers to access information relating to compliance with the conditions of the exemption with respect to transactions made by individual participants is contrary to the interests of plans and participants. Also, allowing plans to have access to details about particular transactions in this manner could be interpreted as imposing a new affirmative duty on the plan to ensure that the conditions of the applicable exemption have been fully satisfied. We do not believe this is an appropriate burden to place

[115] 84-24 Proposal, at 76030.

[116] *Id.*

on plans. Similarly, putting plans in this position would also be inconsistent with the rights of participants to make their own decisions about how to manage their own retirement savings accounts.

VIII. Additional Comments on the 84-24 Proposal

PTE 84-24 has been in place for more than 45 years (dating back to the issuance of its predecessor, PTE 77-9). The Department has provided no evidence of circumstances arising during that time under which the Department or other authorities have found that retirement savers were harmed or inadequately protected as a result of actions taken by fiduciaries or non-fiduciary parties-in-interest in compliance with the conditions imposed under the current version of the exemption.

Despite this fact, the 84-24 Proposal would, in effect, revoke the relief provided for investment advice fiduciaries under the current version of the exemption and replace it with an entirely new framework. These changes to PTE 84-24 are not necessary or appropriate without sufficient evidence of a need or problem.

A. The Strict and Narrow Limitations on Eligibility for Exemptive Relief Under the 84-24 Proposal are Arbitrary and Capricious.

Under the 84-24 Proposal, the exemptive relief provided under PTE 84-24 for providers of fiduciary investment advice would only be available to Independent Producers for Insurance Sales Commissions in connection with recommendations of annuities that are not regulated as securities by the SEC. In all other circumstances, PTE 2020-02 would be the sole source of exemptive relief available to investment advice fiduciaries. For the reasons presented in the following sections, these limitations are arbitrary and capricious.

1. Overly Narrow Definition of Independent Producer

The definition of "Independent Producer" in the 84-24 Proposal is too narrowly tailored and would leave many producers without access to a workable exemption. For example, the definition of Independent Producer would seemingly not include "captive" or "career" producers who are employees of one insurer but are authorized to sell a diverse mix of both proprietary (either to carrier or distributor) and national products, including other insurers' products. Moreover, comments in the preamble indicating that only "an independent, insurance-only agent" would be eligible to rely on the revised exemption[117] raises a question as to whether the definition would include registered representatives of broker-dealers who are

[117] *Id.*, at 76008.

permitted by their firms to sell fixed and indexed annuities away from the broker-dealer as outside business activities.[118]

In each of these circumstances, the producer's employer would face the same challenges as an insurer whose products are sold through a financial professional who falls within the current definition. Excluding such producers from eligibility for relief under the exemption would be arbitrary and capricious.

In addition, PTE 84-24 is often used as a preventative measure by insurance producers who do not believe they are fiduciaries but want to avoid violating the prohibited transaction rules in case they are later found to have inadvertently triggered fiduciary status. Due to the fiduciary acknowledgment requirement in the 84-24 Proposal, the exemption would no longer be available for use in this manner. Allowing the use of the exemption in this manner would result in greater protection for retirement savers, as financial professionals would have an incentive to comply with the exemption's conditions even where fiduciary status has not been definitively established.

2. Overly Narrow Definition of Insurance Sales Commission

The definition of "Insurance Sales Commission" in the 84-24 Proposal would arbitrarily and needlessly prohibit a wide variety of different forms of compensation that are common in the marketplace, even where such practices are consistent with a best interest standard. For example:

- Many Independent Producers rely on marketing support, lead generation, technological assistance, back office and compliance support, and practice building services provided by independent marketing organizations in connection with annuity sales. In the absence of these services, many Independent Producers would not survive.
- Many insurers maintain "career" or "captive" agent sales forces who promise to devote all or substantially all their sales efforts to the insurer's products. In exchange for that commitment, and to maintain a highly trained and professional sales force, insurers typically provide captive agents with various benefits subject to continuing production and service requirements, such as health and retirement plan coverage and contributions, office allowances, travel expense reimbursements, and other benefits customary in the industry.

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118 Under the federal securities laws, firms are not required to supervise outside business activities. Many firms are likely to discontinue the practice of allowing registered representatives to sell fixed and indexed annuities if they would be required to take on co-fiduciary status and supervisory responsibility for such transactions under PTE 2020-02.

In both circumstances, the services and benefits provided to financial professionals would seemingly be treated as cash or non-cash compensation under the Fiduciary Definition Proposal. As such, the exclusion of the value of such services from coverage under the 84-24 Proposal would effectively prohibit the use of PTE 84-24 by Independent Producers who rely on those services and benefits to operate their businesses despite the absence of any evidence that such services and benefits could result in harm to retirement savers.

By contrast, the NAIC Model allows for assistance with marketing, office support, retirement benefits, or other reasonable compensation as long as those benefits are not based on the volume of sales of a specific annuity within a limited period of time. Reg BI takes a similar approach. There is no indication in the preamble to the 84-24 Proposal to suggest that the Department considered this alternative approach.

Moreover, longstanding guidance from the Department makes clear that PTE 84-24 is not limited to traditional commissions and can be used for a wide range of forms of compensation.[119] The industry has operated in reasonable reliance on this guidance for many years and, to our knowledge, there is no evidence that retirement savers have been harmed as a result.

The limitation on the types of compensation for which relief is available under PTE 84-24 is also arbitrarily and capriciously inconsistent with PTE 2020-02, both in its current form and as proposed to be amended in the 2020-02 Proposal. PTE 2020-02 can be used for all forms of compensation as long as the applicable conditions are satisfied. The Department has offered no justification for this disparate treatment. In fact, as explained further below, limiting the types of compensation for which PTE 84-24 can be used when PTE 2020-02 can be used for all forms of compensation directly contradicts the Department's pursuit of a "level playing field."

3. *Overly Narrow Limitation on Types of Products Eligible for Relief*

All fixed and variable annuities, whether registered as securities or not, are insurance products that provide protected lifetime income and therefore should be treated the same under PTE 84-24. Given the need for a level playing field for all annuities, exemptive relief should be available for sales of both variable annuities and fixed annuities to IRAs under both PTE 84-24 and PTE 2020-02.

For decades, PTE 84-24 has been the primary pathway for exempting the sale of annuity and insurance products to plans, including IRAs, and IRI believes it should continue to be available

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[119] Letter from U.S. Dep't. of Lab. and I.R.S. to John A. Cardon et. al., 1977 ERISA LEXIS 87 (October 31, 1977) ("[T]he focus of the disclosure requirement…is upon the entire commission paid by the insurance company in connection with the transaction for the purchase by the plan of the insurance or annuity contract. However,… compensation paid by an insurance company pursuant to a bonus, contingency, override or similar arrangements…would be subject to disclosure…")

to exempt the sale of all such products. Under the 84-24 Proposal, transactions involving sales of variable annuities would no longer be eligible for this exemption. The Department has not provided any evidence to support the need for this disparate treatment.

PTE 2020-02 is available to cover the sale of both fixed and variable annuity products. Such even-handed treatment facilitates the application of uniform sets of exemptive relief conditions to sales of annuity contracts of all types, whether fixed or variable, and should prevail under PTE 84-24 as well. Given the purported alignment between these exemptions under the Proposal, arbitrarily limiting the types of annuity products for which PTE 84-24 can be used would provide no greater level of protection for retirement savers.

The Department's approach to the 84-24 Proposal appears to be based on an inaccurate perception that variable annuities are nothing more than a "package" or "bundle" of mutual funds. IRI strenuously rejects this notion. As with fixed annuities, the protected lifetime income features of variable annuities are the primary attribute of the product, not the investment features. In that vein, IRI observes that variable annuity contracts have more in common with fixed annuity contracts than mutual funds.

B. The 84-24 Proposal Would Not Achieve the Department's Goal of a Level Playing Field.

The Department has argued that PTE 84-24 needs to be amended to align more closely with PTE 2020-02 to provide a level playing field. As explained in more detail in Section X.A. below, ERISA does not require a level playing field but is designed to give the Department flexibility to tailor the conditions for exemptive relief to match the specific circumstances to which that relief would apply. The fact that the Department has created a newer exemption that includes conditions that are not part of PTE 84-24 does not mean that PTE 84-24 must be updated to align with the newer exemption.

Even if we put that fact aside, however, the 84-24 Proposal would fail to produce the level-playing field sought by the Department as a result of the arbitrary and problematic distinctions between the two exemptions, as described above. These distinctions would result in competitive disadvantages for those who operate under PTE 84-24.

C. PTE 84-24 Would No Longer Be Administratively Feasible with the Overly Burdensome and Unworkable Conditions Contemplated by the 84-24 Proposal.

As noted above, the 84-24 Proposal would impose significant new conditions on eligibility for exemptive relief under PTE 84-24 in the context of fiduciary investment advice. Many of these conditions would be so overly burdensome and unworkable as to render the exemption administratively unfeasible for Independent Producers to implement and the Department to regulate and enforce. For example:

- The rollover disclosures contemplated by the 84-24 Proposal would require Independent Producers to compare annuities with securities products, but the federal securities laws prohibit individuals from recommending or providing detailed information or advice about securities without a securities license. Independent producers who are not also securities-licensed (as most are not) would be forced to either break the law to comply with this condition or undertake the expense and burden of obtaining the appropriate securities license(s).[120]

- The 84-24 Proposal would require Independent Producers to disclose all the products and services they are authorized to sell. Producing such disclosures would be extremely time-consuming (much more than the Department has assumed in its Regulatory Impact Analysis), particularly given the frequency with which this information can potentially evolve as producers expand or narrow their offerings to align with the evolving needs of their clients. The Department has offered no compelling explanation as to why this information should have to be proactively provided to retirement savers rather than providing such information upon request.

  Moreover, we fear that many retirement savers would be overwhelmed by the breadth of products and services offered by their preferred financial professional. They would be better served by allowing financial professionals to make case-by-case determinations as to which products and services to discuss with particular retirement savers.

- As the Department has recognized, many Independent Producers are authorized to sell products issued by multiple insurers. In practice, each insurer would develop policies and procedures to comply with the requirements of the exemption based on its own interpretations of the exemption, its own business practices, and its own overall compliance policies and procedures. As a result, Independent Producers would have to figure out how to operate within the different policies and procedures developed by different insurers. This, along with other requirements in the 84-24 Proposal (such as the requirement to disclose all products and services they are authorized to sell), will drive many Independent Producers to reduce the number of insurers for whom they sell and the number of different products they can recommend, not based on the needs of their clients but rather on the need to streamline and simplify their compliance obligations. This would not be in the interest of retirement savers.

- While the 84-24 Proposal would not require Insurers to acknowledge fiduciary status, the supervisory responsibilities imposed on Insurers appear to be nearly indistinguishable from the responsibilities imposed on co-fiduciary Financial Institutions

[120] The 2020-02 Proposal includes similar rollover disclosure requirements, and therefore, Independent Producers who may choose to rely on PTE 2020-02 rather than PTE 84-24 would encounter the same dilemma in that context.

under the 2020-02 Proposal. In light of the Department's assertion in the preamble to the Fiduciary Definition Proposal that "ERISA has a functional fiduciary test and imposes fiduciary status only to the extent the functional test is satisfied," IRI is concerned that compliance with the supervisory responsibilities included in the 84-24 Proposal would expose Insurers to a risk that fiduciary status could be imposed on them even in the absence of a fiduciary acknowledgment.

- The 84-24 Proposal would require that Insurers review every recommendation before issuing the recommended annuity. Given the sheer volume of annuity transactions, this would be impossible. Insurers have a wide variety of tools and techniques at their disposal to appropriately supervise recommendations of their products without necessarily conducting a detailed review of every individual transaction. For example, many insurers use technology to screen transactions to identify circumstances in which closer review may be warranted while allowing transactions that do not trigger any concerns to proceed in due course. In addition, many insurers contract with third parties to perform the supervisory functions required under the NAIC Model. These and other tools and techniques have proven effective to protect consumers, but the Department does not appear to have considered allowing the use of such tools and techniques as an administratively feasible alternative to the approach taken in the 84-24 Proposal.

- The 84-24 Proposal would require that Insurers review recommendations to ensure compliance with the Impartial Conduct Standards and the other conditions of the exemption. However, as the Department acknowledges in the preamble to the 84-24 Proposal, "insurance companies working with independent agents have much less authority over the conduct and compensation of independent agents [and] do not have the necessary control over the independent agents to manage the independent agent's product offerings and do not know the full range of products the independent agent is authorized to sell."[121] Given this reality, insurers would not have access to the information they would need to effectively ensure that Independent Producers have fully complied with the Impartial Conduct Standards and the other exemption conditions.

- The 84-24 Proposal would require Insurers to establish and implement a process to assess whether an Independent Producer can be relied upon to adhere to the Impartial Conduct Standards and to take action as necessary to protect retirement savers against Independent Producers who have failed or are likely to fail to adhere to the Impartial Conduct Standards. However, producer licensing and appointments are governed by applicable state insurance laws and regulations as well as by the terms of contracts that

[121] 84-24 Proposal, at 76005.

may exist between insurers and producers. Depending on the particular circumstances, an insurer may not be able to take the actions contemplated by this provision without violating state law and/or contractual obligations. Moreover, for the same reasons outlined above, insurers would not have access to the information they would need to effectively assess whether any particular Independent Producer can be relied upon to adhere to the Impartial Conduct Standards.

- The retrospective review provision in the 84-24 Proposal would seemingly require every Insurer to conduct an individualized review of each Independent Producer who sold one of the Insurer's products in the prior year "to detect and prevent violations of, and achieve compliance with the conditions of the exemption, including the Impartial Conduct Standards."[122] The findings of this review are required to be detailed in individualized reports that must be provided to each Independent Producer. Insurers typically have tens of thousands of individual producers who are licensed and appointed to sell their products across the country. Requiring individualized reviews and reports for each appointed producer is unnecessary, impractical, and not administratively feasible.
- Moreover, the 84-24 Proposal only requires Independent Producers to share with the Insurer its "conclusion as to whether the recommended annuity is in the Best Interest of the Retirement Investor" in section VII(b)(6) and the rollover documentation in section VII(b)(7). This level of information would be wholly inadequate to conduct the required retrospective review effectively.
- The 84-24 Proposal would require Insurers to conduct separate retrospective reviews (or sub-reviews) for each Independent Producer that has sold any business in the period covered by the review. Many Insurers would have supervisory obligations over thousands of Independent Producers if the 84-24 Proposal is adopted, which would require Insurers to conduct and document thousands of individual retrospective reviews. This would be impossible without investing many multiples of the time and resources estimated by the Department.
- Under the 84-24 Proposal, an Independent Producer would be allowed to make the corrections needed to avoid a nonexempt prohibited transaction. Self-correction would be allowed when either (1) the Independent Producer has refunded "any charge" to a retirement saver, or (2) the Insurer has rescinded a mis-sold annuity, canceled the contract, and waived the surrender charges. The Independent Producer would be required to notify the Department of the violation and the opportunity for a refund or

[122] 84-24 Proposal, at 76028-76029.

rescission via email within 30 days of correction. In addition, the Independent Producer would be required to notify the person(s) at the Insurer responsible for conducting the retrospective review during the applicable review cycle and the violation and correction must specifically be set forth in the written retrospective review report.[123]

In general, we support allowing for self-correction to preserve reliance on PTE 84-24. However, it appears that self-correction would be expected whenever an Independent Producer refunded any charge to the retirement saver, regardless of the amount refunded. The absence of a materiality threshold would make the self-correction provision administratively unfeasible, as the Department and the Insurer would have to be notified of each and every instance in which any amount is refunded to the retirement saver.

It appears that the Department did not consider the inclusion of a materiality qualifier that would allow *de minimis* refunds (e.g., those below a certain dollar amount) to be made without notification to the Department and the Insurer while still maintaining reliance on PTE 84-24. Such a provision would reduce the scenarios in which Independent Producers have to provide notifications, in circumstances where the absence of notification would not deprive the Insurer and the Department of meaningful information.

IX. Additional Comments on the 2020-02 Proposal

A. <u>The Department Failed to Appropriately Consider Reasonable Alternatives to the Approach Taken in the 2020-02 Proposal.</u>

The preamble to the Fiduciary Definition Proposal asserts that:

> PTE 2020–02 is consistent with the requirements of the SEC's Regulation Best Interest and the fiduciary obligations of investment advisers under the Advisers Act. Therefore, broker-dealers and investment advisers that have already adopted meaningful compliance mechanisms for Regulation Best Interest and the Advisers Act fiduciary duty, respectively, should be able to adapt easily to comply with the PTE.[124]

Senior Department officials have emphasized this point in recent public statements, claiming that firms and financial professionals operating in compliance with Reg BI should have no problem satisfying the changes contemplated by the 2020-02 Proposal. However, the 2020-02 Proposal includes extensive requirements that go far beyond the requirements of Reg BI. If the Department's intent is to align PTE 2020-02 with Reg BI, it should have considered providing a

[123] 84-24 Proposal, at 76029.
[124] Fiduciary Definition Proposal, at 75899.

safe harbor for Reg BI compliance as a reasonable alternative to the approach taken in the 2020-02 Proposal. There is no indication in the preamble to the 2020-02 Proposal or anywhere else in the Proposal that the Department considered this alternative.

B. The 2020-02 Proposal Would Render PTE 2020-02 Unworkable for Insurers in the Institutional Market.

PTE 2020-02 and the changes contemplated by the 2020-02 Proposal are designed for transactions involving retail customers. The conditions in the exemption, such as the required compensation disclosure, would not be workable in the context of transactions between institutions. The Department has provided no compelling reason to hold providers of advice to plans and their fiduciaries to the same rules as those who provide advice to individual retirement savers. On the contrary, doing so would harm plans and plan fiduciaries by making it more difficult for them to obtain the services they need to effectively serve plan participants.

X. Comments on the Other PTEs Proposal

A. The Other PTEs Proposal is Impermissible Under ERISA § 408(a).

Under the Other PTEs Proposal, investment advice fiduciaries would no longer be eligible for exemptive relief under PTEs 75-1, 77-4, 80-83, 83-1, and 86-128. Instead, fiduciaries would be forced to rely on the revised versions of either PTE 2020-02 or PTE 84-24. The Department has asserted that this one-size-fits-all approach to exemptions is necessary to ensure a level playing field for all investment advice fiduciaries and to avoid regulatory arbitrage. However, ERISA does not require a level playing field or charge the Department with responsibility for avoiding regulatory arbitrage. In fact, we believe ERISA actually requires that the Department tailor exemptions to the particular circumstances in which exemptive relief is needed.

ERISA §408(a) authorizes the issuance of conditional or unconditional exemptions for any class of fiduciaries or transactions from all or part of the restrictions imposed by ERISA Sections 406 and 407(a). An exemption can only be issued upon a finding that the exemption is (1) administratively feasible, (2) in the interests of the plan and its participants and beneficiaries, and (3) protective of the rights of participants and beneficiaries of such plan. The Other PTEs Proposal fails to satisfy the requirements of ERISA §408(a) for several reasons:

i. By authorizing the issuance of exemptions for "any fiduciary or transaction, or class of fiduciaries or transactions," Congress made clear that exemptions should be designed for the particular circumstances in which they would be used. The Department has recognized and understood this for nearly a half-century, as evidenced by the issuance of countless individual and class exemptions that were specifically tailored. Importantly, we believe the Department has appropriately considered the overall regulatory frameworks that govern the conduct of different investment advice fiduciaries when crafting the existing exemptions. For example, mutual funds and annuities are heavily regulated by well-established agencies under strong and effective rules, while the rules for cryptocurrency are still under development. More vigorous rules may be appropriate in some cases, but there is no need to impose extensive new burdens on well-regulated products. Treating all investment advice fiduciaries alike, as contemplated by the Proposal, overlooks these significant and relevant differences.

ii. The changes contemplated by the Other PTEs Proposal would require these firms and financial professionals to discontinue using their existing and effective policies, procedures, and systems and to undertake extensive, costly, and time-consuming efforts to develop new policies, procedures, and systems to satisfy the conditions of PTE 2020-02 or PTE 84-24. To assert that such a massive project is somehow administratively feasible seems to reflect a serious misunderstanding of the concept of feasibility.

iii. Given the lack of evidence that retirement savers are being harmed under the current framework, it is clear and obvious to us that plans and participants will be no more effectively protected if the Proposal is adopted in its current form. In fact, many plans and participants will be harmed by the Other PTEs Proposal, as it will surely cause some firms and financial professionals to make the difficult decision to discontinue serving retirement savers rather than taking on the massive and costly work that would be needed to transition from their existing exemptions to PTE 2020-02.

B. <u>The Other PTEs Proposal is Arbitrary and Capricious.</u>

Depriving investment advice fiduciaries of access to PTEs 75-1, 77-4, 80-83, 83-1, and 86-128 is arbitrary and capricious. These exemptions have been in place for decades, and as required by ERISA §408(a), each is designed for a particular class or classes of fiduciaries or transactions:

i. PTE 75-1 Part I provides relief for agency transactions and services.

ii. PTE 75-1 Part II(1) permits the purchase or sale of a security between an employee benefit plan or IRA and a broker-dealer, a reporting dealer who makes primary markets in securities of the United States Government or of any agency of the United States Government and reports daily to the Federal Reserve Bank of New York its positions with respect to Government securities and borrowings thereon, or a bank supervised by the United States or a State.

iii. PTE 75-1 Part II(2) contains a special exemption for mutual fund purchases between fiduciaries and plans or IRAs.

iv. PTE 75-1 Part III permits a fiduciary to cause a plan or IRA to purchase securities from a member of an underwriting syndicate other than the fiduciary itself when the fiduciary is also a member of the syndicate.

v. PTE 75-1 Part IV permits a plan or IRA to purchase securities in a principal transaction from a fiduciary that is a market maker with respect to such securities.

vi. PTE 75-1 Part V permits the extension of credit to a plan or IRA by a broker-dealer in connection with the purchase or sale of securities.

vii. PTE 77-4 provides relief for a plan's or IRA's purchase or sale of open-end investment company shares where the investment adviser for the open-end investment company is also a fiduciary to the plan or IRA.

viii. PTE 80-83 provides relief for a fiduciary causing a plan or IRA to purchase a security when the issuer may use the proceeds of the securities issuance to retire or reduce indebtedness to the fiduciary or an affiliate.

ix. PTE 80-83 provides relief for the sale of certificates in an initial issuance of certificates by the sponsor of a mortgage pool to a plan or IRA when the sponsor, trustee, or insurer of the mortgage pool is a fiduciary with respect to the plan or IRA assets invested in such certificates.

x. PTE 86-128 provides relief for certain types of fiduciaries to (a) use their authority to cause a plan or IRA to pay a fee to the fiduciary, or its affiliate, for effecting or executing securities transactions as agent for the plan, and (b) act as agent in an "agency cross transaction" for both a plan or IRA and one or more other parties to the transaction, and for such fiduciaries or their affiliates to receive fees from the other party(ies) in connection with the agency cross transaction.

Firms and financial professionals have relied upon these exemptions in good faith and have expended significant time and resources to develop and maintain policies, procedures, and systems tailored to the specific conditions and requirements of each exemption. The Department has offered no evidence of harm to retirement savers who have received fiduciary investment advice under these exemptions. Upending these long-standing and effective PTEs in pursuit of a "level playing field" – which, as noted above, is neither required by nor consistent with ERISA §408(a) – would be the epitome of arbitrary and capricious rulemaking.

XI. Comment on the Timeline for Effectiveness and Implementation

A. <u>The Proposed Effective Date is Arbitrary and Capricious, and Impermissible Under ERISA §408(a).</u>

The Department has significantly underestimated the amount of time annuity providers and distributors would need to come into compliance with the rule changes reflected in the Proposal. It would be impossible for most, if not all, our members to fully assess and implement the highly complex requirements and conditions included in the Proposal in just sixty days. Past

Department rulemaking projects have provided far longer implementation periods, ranging from eight months for the 2016 Rule (which was itself inadequate in light of the extremely challenging and complex requirements of that rule, and was eventually extended through a non-enforcement policy adopted by the Department) to two years for the service provider disclosure regulations under ERISA §408(b)(2).

Despite the Department's assertion that the Proposal is intended to align with other existing standard of conduct regulations, such as Reg BI, a firm could not assert that they are in compliance with the ERISA fiduciary standard based on their compliance with Reg BI. Many firms and financial professionals would be subject to this standard for the first time as a result of the Proposal and would therefore have to significantly overhaul their policies, procedures, and information technology systems to ensure compliance with that standard.

Even firms and financial professionals already operating under the current version of PTE 2020-02 would have to undertake extensive revisions to their policies and procedures and perform costly and time-consuming information technology re-designs and build-outs. Many companies would not be able to meet the Proposal's requirements within such a short time frame and would be forced to suspend delivery of services to customers in order to avoid violating the conditions of the exemption (and, by extension, to avoid the risk of losing eligibility to rely on the exemption based on such violations under the draconian disqualification provision). As a result, many plans, participants, and beneficiaries would immediately be left without access to much-needed professional guidance and advice until the necessary work can be completed.

Relatedly, compliance efforts will be complicated and challenged by the absence of grandfathering protection for conduct occurring before the Proposal takes effect.

The Department has offered no compelling rationale for this extraordinarily compressed, unworkable, and unprecedented implementation timeline, and as such, we believe this timeline is arbitrary and capricious. Moreover, it would not be administratively feasible or in the interests of plans and participants to require implementation of the changes being made to PTE 2020-02, PTE 84-24, and the other exemptions to be amended under the Proposal, and therefore violates the requirements of ERISA §408(a).

XII. Comments on the Department's Regulatory Impact Analysis

A. <u>The Department's Regulatory Impact Analysis Relies on Stale and Inaccurate Data</u>.

The Department's regulatory impact analysis (the "<u>RIA</u>"), as presented in the preamble to the Fiduciary Definition Proposal, includes no real-world evidence or data showing that retirement savers are being harmed as a result of deficiencies in the current regulatory framework. Such evidence would be difficult to produce given that Reg BI, the NAIC Model, and 2020-02 have only been in place for a relatively short period of time. In place of current data and information, the RIA relies on stale data used by the Department to support the 2016 Rule.

Most notably, the RIA recycles the assertion made in 2015 by the President's Council of Economic Advisers that $17 billion in annual IRA losses can be attributed to conflicts of interest.[125] This assertion is extremely misleading and has no basis in fact. It is simply one percent of the total retirement savings in the United States in 2015. No evidence was provided at that time or since to support the implication that all advice received by retirement savers is conflicted.

B. The Department's Regulatory Impact Analysis is Littered with Wholly Unreasonable and Inaccurate Assumptions.

The RIA is largely based on the Department's own estimates and assumptions as to the costs and benefits likely to result if the Proposal is adopted in its current form. However, many of the Department's estimates and assumptions are highly flawed and inaccurate. For example:

- The RIA significantly underestimates the costs and risks associated with taking on fiduciary status under Title I of ERISA. The expansiveness of the Fiduciary Definition Proposal means that many firms and financial professionals would find themselves subject to fiduciary status for the first time. The RIA is based on estimates of time and cost that do not come close to accurately reflecting the actual amount of time and money that would be needed to perform the extensive work necessary to implement and comply with the Proposal.
- The RIA severely underestimates how many Independent Producers sell annuities and would potentially need exemptive relief under PTE 84-24 if the Proposal is adopted. The actual number of Independent Producers is nearly 20 times the number included in the RIA. The RIA also fails to consider the implications for Independent Producers who may need to rely on third parties to perform some or all the work necessary to implement and comply with amended PTE 84-24, which could potentially be treated as cash or non-cash compensation for which exemptive relief would be needed.
- The RIA incorrectly assumes that all eligible entities currently rely on PTE 2020-02 and would continue to do so if the Proposal is adopted. Our understanding is that some eligible entities do rely on PTE 2020-02, but a meaningful number of eligible entities have either determined that their conduct does not trigger fiduciary status in the first place or opted to modify their business practices to avoid triggering fiduciary status or to avoid engaging in prohibited transactions for which exemptive relief under PTE 2020-

[125] Council of Economic Advisors, *The Effects of Conflicted Investment Advice on Retirement Savings* (2015), https://obamawhitehouse.archives.gov/sites/default/files/docs/cea_coi_report_final.pdf.

02 would be required. The Proposal would, in our view, make this course of action far less viable, meaning that some eligible entities who do not currently rely on PTE 2020-02 would be compelled to do so. These entities would have to incur many, if not all, of the same costs and burdens as entities that implemented PTE 2020-02 prior to the issuance of the Proposal. These costs are not taken into account in the RIA.

- The RIA incorrectly assumes that implementation of the changes reflected in the 2020-02 Proposal will be relatively simple and easy to implement based on an assertion that the revised version of the exemption would closely align with Reg BI. However, as we explain above, this is not true. The 2020-02 Proposal includes significant changes that go well beyond the requirements of Reg BI. Significant amounts of time, money, and resources would be needed to implement and comply with the material differences between Reg BI and the 2020-02 Proposal.

C. The Department's Regulatory Impact Analysis Ignores Critical Factors and Information.

The RIA is based almost exclusively on research, data, information, and evidence that purportedly supports the Proposal. Rather than considering all relevant research, data, information, and evidence to achieve the best outcome for retirement savers, the Department seemingly elected to disregard any contradictory data and evidence in order to move forward with the Proposal. For example:

- The RIA includes no compelling evidence to suggest that the changes contemplated by the Fiduciary Definition Proposal and the 2020-02 Proposal are necessary to address deficiencies or problems with the current definition of fiduciary or the current version of PTE 2020-02, respectively.
- The RIA briefly acknowledges and quickly dismisses significant real-world evidence of the widespread harm suffered by retirement savers due to the 2016 Rule.[126] Reputable studies by well-respected research organizations found that at least 10.2 million retirement savers lost access to financial advice in 2016. The Department asserts that this inconvenient data is inaccurate but offers no evidence to support its view.
- The RIA fails to adequately account for the value of financial advice or the long-term value of annuities and insurance products. Instead, the RIA focuses only on the costs associated with such products and related services provided by firms and financial professionals and therefore significantly underestimates the potential benefits of taking no action and overestimates the potential benefits that would result from the Proposal.

[126] *See, e.g.,* the Chamber Report and the Deloitte Report.

 - For example, the RIA cites a 2007 study by Friesen and Sapp to assert that equity mutual fund investors experience an average 1.56 percent return reduction and that poor market timing stems from broker advice. If this is true, then not timing the market poorly should preserve that 1.56 percent, and variable annuities with protected lifetime income benefits generally prevent this reduction due to poor market timing by requiring investment in an asset allocation fund or adherence to a model portfolio with periodic automatic rebalancing, partially offsetting the additional fees associated with the variable annuity and the income guarantee. Further, a 2022 Dalbar study found that the average equity subaccount investor outperformed the average equity mutual fund investor by 3.5 percent due to this effect, with equity subaccount investors exhibiting retention rates up to 1.38 years longer than equity mutual fund investors.[127]
 - The costs involved with having access to a financial professional in the context of a rollover IRA cannot be compared to the costs of investment options in a workplace defined contribution plan. This is akin to comparing a full-service hotel to a hostel and concluding the hotel is unsuitable because a stay costs more. Access to a financial professional is not typically available to workplace plan participants but is available in the context of an IRA rollover. The financial professional should be compensated for those services, and the financial professional and the retirement saver should be free to decide whether that relationship should be ongoing or transactional.

- The RIA clearly demonstrates the Department's lack of expertise and experience regarding annuity products and annuity distribution channels.
  - The RIA asserts that "overpriced" annuities are commonly used in IRA rollovers and that this harms retirement savers but provides no benchmark or basis upon which to determine whether an annuity is overpriced or not. An in-plan index fund with a 25 basis point management fee cannot be compared to an annuity that may carry three to four percent in total annual charges but is professionally managed and provides lifetime income protection.
  - The RIA takes pains to note that I-share sales of variable annuities fell following the vacatur of the 2016 Final Rule in 2018, yet the percentage decrease is both inaccurate and misleading. According to Morningstar data, I-share sales fell 15 percent in 2019, to $5.8 billion from $6.8 billion, were unchanged in 2020, and actually doubled in 2021 to $10.2 billion due to a strong equities market

[127] DALBAR, Inc., *2022 Quantitative Analysis of Investor Behavior - Variable Annuities*.

performance in 2021. Moreover, citing only percentage increases neglects to acknowledge that fee-based variable annuity sales currently account for less than 2 percent of total annuity sales.

- The RIA posits a $6.6 billion increase in annual returns from an average 30 basis point reduction in fees if all $2.2 trillion in total variable assets in 2018 were moved to low-fee variable annuities, but this ignores the fact that low-cost annuities either do not offer lifetime income protections or offer them for an additional fee, which is not reflected in the analysis. It also ignores the fact that approximately $400 billion of the $2.2 trillion is in fixed accounts which carry no fee, and another $300 billion is in group contracts.
- The RIA displays a fundamental ignorance regarding fixed indexed annuities through the statement, "...the terms in the contract and the method used to calculate gains and losses MAY [emphasis added] result in actualized gains and losses that differ from the gains and losses experienced by the index." [128] This is not a "may," this is a "will." The basic structure of an fixed indexed annuity would make it impossible to credit the full gain of the index to the contract, as only a portion of the premium is used to purchase options on one or more market indexes. Moreover, the value proposition of fixed indexed annuities for retirement savers is that they provide downside protection in exchange for limitations on upside potential. As required under state law, purchasers of fixed indexed annuities are provided with clear disclosures explaining how the products work, including the limitations on gains and losses. Depicting index performance above and beyond the specified limitation on gains as equivalent to investment losses, as implied in the RIA, is inaccurate and irresponsible.

XIII. Conclusion

In an age when saving and preparing for retirement is squarely on the shoulders of individuals, financial professionals play an important role in helping their clients develop retirement plans and grow their savings. As currently formulated, the Proposal will deprive lower- and middle-income retirement savers of access to affordable guidance with retirement planning. For all the reasons expressed above, we urge the Department to withdraw the Proposal and discontinue its efforts to change the definition of fiduciary investment advice and the existing exemptions relied upon by investment advice fiduciaries. Instead, the Department should direct its time and resources to initiatives that will improve retirement security, such as implementation of the SECURE Act of 2019 and the SECURE 2.0 Act of 2022.

[128] Fiduciary Definition Proposal, at 75928.

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Thank you again for the opportunity to provide these comments. If you have questions about our comments on the Proposal or if we can be of any further assistance in connection with this matter, please feel free to contact the undersigned at wchopus@irionline.org or jberkowitz@irionline.org.

Respectfully submitted,

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Attachments

CH 4

Annuities 101

What Is an Annuity?

Annuities have been around for centuries. In early Roman times, citizens would make a one-time payment to a contract known as an *annua* in exchange for income payments received once a year for the rest of their lives. Today, an annuity is an insurance agreement that comes in a number of different forms and can (1) help individuals accumulate money for retirement through tax-deferred savings, (2) provide them with monthly income that can be guaranteed to last for as long as they live, or (3) do both.

An annuity can be viewed as life insurance in reverse. Whereas life insurance protects a family's financial situation against the premature death of a breadwinner, an annuity protects an individual or a couple from running out of money at an advanced age. As with life insurance, annuity contracts are based on the principle of risk pooling; that is, the pooled funds of a large group are used to pay benefits to a relative few in any given year. The burden of not knowing how long one will live is shifted from the individual to the insurance company, which spreads the longevity risk among all annuitants, some of whom will die sooner than expected while others will live longer than expected. A good analogy is homeowner's insurance: the risk of fire is common to all homeowners, but during a given span of time only a few houses will burn down. For most people such an event would be financially devastating, so the risk is pooled using insurance.

Annuities can play a vital role in helping investors save for retirement and receive guaranteed lifetime income during retirement — effectively giving them the ability to create their own pensions. Unlike other investments, annuities provide a wide variety of benefit options that can protect against untimely death, provide principal guarantees, assure a specified amount of income when the contract is annuitized, guarantee withdrawals for life, or a combination of all of these.

What Role Can Annuities Play in a Comprehensive Retirement Plan?

Annuities are the only financial instruments available today, other than Social Security and employer-provided pensions, that can guarantee a lifetime stream of income during retirement. Along with giving retirees the peace of mind that comes from knowing they will not outlive their assets; annuities provide another important benefit — a way to increase current income.

Many of today's retirees are faced with the challenge of how to withdraw enough money from their portfolios to live comfortably during retirement without depleting their funds if they live a long life. Withdrawing money from an investment portfolio may not present a problem in the early years, but as retirees age, the risk of running out of money can increase dramatically. Allocating a portion of the portfolio to one or more annuities reduces this risk.

Annuity payments form an essential part of a comprehensive retirement plan along with Social Security and pension income. The amount of each annuity payment reflects the fact that some annuitants will not live as long as others. This "risk pooling" allows insurance companies to make annuity payments that are larger than would be possible through a systematic withdrawal plan, where an individual retiree periodically withdraws funds in amounts that give reasonable assurance that he or she will not run out of money. Thus, annuities can serve to both reduce the risk of running out of money in retirement and increase the amount of each income payment received.

Who Are the Parties to an Annuity Contract?

Most annuity contracts — and all commercial annuity contracts — are issued by life insurance companies. When the purchaser completes the application to buy an annuity, the contract owner, annuitant, and beneficiary are designated and identified as such in the contract.

Contract Owner

The owner of an annuity contract pays the premiums. He or she has certain rights under the contract, such as the right to make contributions, withdraw all or a portion of the contract value, or change the parties to the contract. The owner is usually an individual or couple but can also be a non-natural person such as a trust or a partnership. Special tax rules apply to annuities owned by non-natural persons.

Annuitant

The annuitant is the person upon whose life annuity payments are based. Often, the annuitant is also the contract owner, so payments continue as long as the owner/annuitant is alive. It is also possible for two people, such as an owner and spouse, to be designated as joint annuitants so that income can continue throughout either of their lives. This type of annuity is called a "joint and survivor annuity." While in most cases payments are made to the contract owner or annuitant, funds also can be paid to a third party referred to as a "payee."

Beneficiary

The beneficiary is the person designated under the contract to receive any payments that may be due upon the death of the contract owner or annuitant. Contingent beneficiaries, to whom payments are made in the event the primary beneficiary predeceases the owner or annuitant, may also be named in the contract.

Respective Rights of the Parties

Because annuity contracts can offer a great deal of flexibility in setting up income payments, the respective rights of the contract owner, annuitant, and beneficiary can vary. For example, under one insurer's contract, the owner may be entitled to receive annuity payments. Under another insurer's contract, the annuitant may be the party entitled to receive annuity payments.

What Types of Annuities Are Available?

A wide variety of annuities are available today, many designed to meet specific needs and help consumers achieve their retirement goals. With a deferred annuity, assets accumulate on a tax-deferred basis until distributions are made, usually during retirement; with an immediate annuity, the contract owner converts assets into income and starts receiving payments right away. Fixed annuities accumulate savings or distribute income at guaranteed rates and in guaranteed amounts; variable annuities accumulate savings or distribute income based on the performance of the underlying investment options chosen by the contract owner. Annuities can be part of an IRA, a qualified retirement plan such as a 401(k) or 403(b) (a "qualified" annuity) or may be purchased with after-tax dollars (a "non-qualified" annuity). The following is a more detailed look at various types of annuities.

Figure 4-1 Types of Annuities

	Deferred	Immediate
Variable (VA)	• Purchased either with a single premium or with periodic payments to help save for retirement; the contract owner determines the point at which accumulated principal and earnings are converted into a stream of income. • The contract value or income payments vary based on the investment performance of underlying subaccounts or a stated rate, if provided by the issuer. • Total sales of deferred VAs in 2022 were $98.6 billion.	• Purchased with a single lump sum; income payments begin within a short period — less than 13 months. • The income payments vary based on the investment performance of underlying subaccounts or a stated rate, if provided by the issuer. • Total sales of immediate VAs in 2022 were about $0.1 billion.
Structured	• Structured annuities, also called Registered Index Linked Annuities (RILAs) use options on market indexes to provide purchases with upside potential and downside protection • RILAs carry investment risk, and are therefore a form of variable annuity • Total RILA sales in 2022 were $36.4 billion (included in deferred VA total sales above)	• There are no immediate versions of RILAs, but as a variable annuity they may be annuitized to create a fixed lifetime income stream
Fixed	• Purchased either with a single premium or with periodic payments to help save for retirement; the contract owner determines the point at which accumulated principal and earnings are converted into a stream of income. • Guarantees that the contract owner will earn a stated rate of interest during the accumulation phase of a deferred annuity and receive a defined amount of income on a regular schedule when the contract is annuitized. • Total sales of deferred fixed annuities in 2022 were $192.2 billion.	• Purchased with a single lump sum; income payments begin within a short period — less than 13 months. • The income payments are a pre-determined amount on a regular schedule. • Total sales of immediate fixed annuities in 2022 were $10.3 billion. • Total sales of deferred income annuities (essentially “immediate” annuities with a five to 40 years waiting period before payments begin) in 2022 were $1.0 billion.

Source: Morningstar, Inc.; Beacon Research

What Are the Differences Between Deferred and Immediate Annuities?

Deferred Annuities: A Way to Save Money for Retirement

Many people buy annuities because they want their money to grow tax-deferred while they are saving for retirement, and they want a guaranteed income stream once they retire. This type of annuity is called a deferred annuity. A deferred annuity contract has two phases — an accumulation or savings phase, and a payout or retirement income phase.

In the accumulation phase, the owner pays premiums (also referred to as purchase payments) into the contract to accumulate assets. Some contracts are purchased with a single payment and are called single premium contracts. Other contracts allow payments to be made at any time and are called flexible premium contracts. During the accumulation phase, the owner can surrender the contract or take one or more partial withdrawals.

In the payout phase, the owner (or other designated payee) receives income. When he or she wants payments to begin, the insurance company starts sending checks on a regular basis, typically monthly. The effective date of payments is called the annuity start date or the annuity commencement date. In certain circumstances, the insurance company will allow annuity payments to be commuted for a lump sum equal to their present value.

Immediate Annuities: When You Want to Receive Money Right Away

An immediate annuity (commonly known by the acronym SPIA, which stands for Single Premium Immediate Annuity, and may also be called a “payout” or “income” annuity) is purchased with a single premium and annuity payments begin right away (there is no accumulation period). If the owner chooses to receive monthly payments, payments usually begin at the end of the first month but may be scheduled to start any time within one year after purchase. An immediate annuity can be purchased using retirement savings, for example, from a 401(k) plan and/or personal savings, as a way to create guaranteed income payments during retirement. It can also be purchased using money from other sources, such as an inheritance or the sale of a business.

Annuity payments can be made over the lives of one or more individuals or for a specified number of years, e.g., for 10 or 15 years. Life annuity payments typically end when the annuitant dies, but various types of guarantees are widely available. For example, you can purchase a life annuity with 10 years of payments guaranteed. Under such an annuity, the payments will continue for the longer of 10 years or the annuitant’s life. In addition, insurers offer annuity payments that provide that if the annuitant dies before annuity payments equal to the premiums paid for the contract have been paid, the contract beneficiary will receive a lump sum equal to the difference between the sum of the annuity payments and the premiums paid (“cash refund”). As there are many payout options offered by issuing insurers, the owner should work with his or her financial advisor to assure that the payment feature meets his or her financial needs.

Data from the CANNEX annuity quoting platform shows about one-third of quote requests, a good proxy for sales, are for SPIA with cash refund, about 20 percent are for life-only payments, and the remaining approximately one-half are for life with periods certain of various durations, 10 years being the most common. More than 85 percent are for monthly payments.

Inflation-Protected Annuities

An inflation-protected annuity (IPA) is similar to an immediate annuity but payments are indexed to the rate of inflation. Initial payments will usually be smaller than they would be without the inflation protection. Even at a moderate rate of 4 percent, inflation reduces the purchasing power of one dollar to fifty cents in approximately 15 years. IPAs guarantee a real rate of return at or above inflation. Very few life insurance companies offer true IPAs for sale in the United States (largely due to the difficulty of hedging the inflation risk). However, consumers can buy immediate annuity contracts available that provide pre-determined annual increases in the amount of annuity payments, e.g., 3 percent each year for the life of the contract. CANNEX data indicates more than 90 percent of quotes include no payment adjustment feature, i.e., no provision for increasing future monthly payments.

Structured Settlement Annuities

Structured settlement annuities are used to provide periodic payments to satisfy legal judgments. Structured settlement sales numbers are not included in the market data used in this publication.

What Are the Differences Between Fixed and Variable Annuities?

Fixed Annuities: Guaranteed Investment Performance

With a fixed annuity, the owner is guaranteed at least a minimum rate of investment return. The insurer declares a specific credited rate of return based on the investment performance of its general account assets. In the case of a deferred fixed annuity, the insurance company guarantees a minimum interest rate (also known as a minimum credited interest rate) on payments made by the owner during the accumulation phase. In many cases, an insurer will credit interest at a higher rate than the minimum for varying periods. This type of interest is often referred to as "excess interest." The owner's purchase payments are invested in the insurance company's general account. When the annuity reaches the payout phase, the dollar amount of the annuity income payments is determined based on payment rates guaranteed at the time the deferred annuity was issued (or the insurer's current payment rates, if higher) and are guaranteed for the selected payout duration, e.g., the owner's life or a specified period of years.

Generally, fixed annuities involve less investment risk than variable annuities because they offer a guaranteed minimum rate of interest. The minimum rate is not affected by fluctuations in market interest rates or the company's yearly profits. Some people like the security of knowing that their annuity payments will never vary or that they will receive at least a minimum amount of credited interest. Although they are less risky, fixed annuities generally offer less investment flexibility and less opportunity for growth than variable annuities.

Fixed Indexed Annuities: Market-Linked Interest Potential and Guaranteed Minimum Interest

A Fixed Indexed Annuity is a fixed annuity that typically provides the contract owner with an investment return that is a function of the change in the level of an index, such as the S&P 500, while guaranteeing no less than a stated fixed return on the investment. These products are designed for investors who want to partake in the benefits of a market-linked vehicle with a protected investment floor if there is a downturn in the benchmark index. Some indexed annuities also offer riders that guarantee income for life, even if the annuity value declines to zero.

Variable Annuities: Investment Performance Based on Portfolios Chosen by the Owner

With a variable annuity, contract owners may choose from a wide range of investment options called subaccounts, each of which generally invests in shares of a single underlying mutual fund or, in some cases, in a “fund of funds (FOF),” which is a mutual fund that invests in several other mutual funds or in exchange-traded funds (ETFs). Variable annuity contract owners may direct the allocation of their contract value among subaccounts that correspond to a wide range of underlying mutual funds, such as equity funds, bond funds, funds that combine equities and bonds, actively managed funds, index funds, domestic funds, and international funds. Unlike mutual funds sold to the public, the mutual funds that underlie subaccounts are available only to investors in variable annuities, variable life insurance contracts, and in some cases, 401(k) plans, IRAs, and certain other investments permitted by applicable tax laws and regulations. Assets in a variable annuity can be transferred between subaccounts tax-free. As a result, investment decisions can be made based on an investor’s needs and strategy without worrying about the tax implications.

As with mutual funds, the investment returns of variable annuity subaccounts fluctuate. During the accumulation phase, the contract value varies based on the performance of the underlying subaccounts. During the payout phase of a deferred variable annuity (and throughout the entire life of an immediate variable annuity), the dollar amount of the annuity payments may also fluctuate if variable annuitization is chosen, again based on how the portfolio performs. Fixed annuitization generally produces equal payments over the time period selected (life only or life in combination with a minimum payment period).

Unlike mutual funds, annuities offer a wide variety of guarantees to protect a contract owner’s investment. Death benefits provide principal protection in the event a contract owner dies during a market downturn. Living benefit features protect against investment and/or longevity risk by providing guarantees that cover income, accumulation, and withdrawals for either a fixed number of years or for life.

In addition to variable investment options or subaccounts, many variable annuities offer a fixed account or fixed investment option. This means that during the accumulation phase of a deferred variable annuity, the owner can allocate payments not only to one or more variable investment options, but to a fixed interest option as well. The money allocated to the fixed option goes into the insurance company’s general account. A minimum rate of interest is typically guaranteed for a period of one or more years.

Registered Index Linked Annuities (RILAs) are a relatively recent innovation. RILAs generally do not offer subaccounts (although some include a money market subaccount); rather, purchase payments are invested in the insurer’s general account, and a portion is used to purchase options on one or more market indexes selected by the purchaser. The use of options provides some upside potential to contract owners in years when the index(es) perform well, and limit downside risk during years when returns are negative.

During the payout phase of some contracts, only fixed annuity income payments are offered. Other contracts provide fixed and/or variable payouts. Providing both types of payouts allows contract owners to take on the added risk associated with variable investment options while accumulating assets, and to manage their level of risk during retirement by choosing to have the rate of return guaranteed for at least some portion of their income payments.

What Are the Differences Between Qualified and Non-Qualified Annuities?

Qualified Plans versus Non-Qualified Plans

Annuities can be used in tax-qualified retirement plans, such as IRAs, pension or profit sharing plans, 401(k) plans, 403(b) plans, and certain governmental plans. These annuities are called qualified annuities and are typically funded with pretax dollars. (Some qualified annuities are purchased with after-tax dollars for use with Roth accounts, under which the annuity payments and other withdrawals are tax-free if certain tax rules are satisfied.) Annuities that are not used in qualified plans are called non-qualified annuities and are purchased by members of the general public with after-tax dollars.

The first variable annuity in America was designed and developed for a qualified retirement program offered by TIAA-CREF (now called TIAA) in 1952. As such, the variable annuity was available only as an investment within a tax-qualified plan until 1960, when the first publicly available variable annuity outside a qualified plan was developed and brought to market by the Variable Annuity Life Insurance Company (VALIC).

An annuity used in a qualified plan can provide contract owners with the same insurance benefits offered by non-qualified annuities, such as guaranteed death benefits, guaranteed living benefits, and guaranteed income payments for life. It does not, however, provide any additional tax-deferred treatment of earnings — tax deferral is provided by the qualified plan itself. (Other tax aspects of qualified and non-qualified annuities are discussed in Chapter 14: *Regulation and Taxation of Annuities.*)

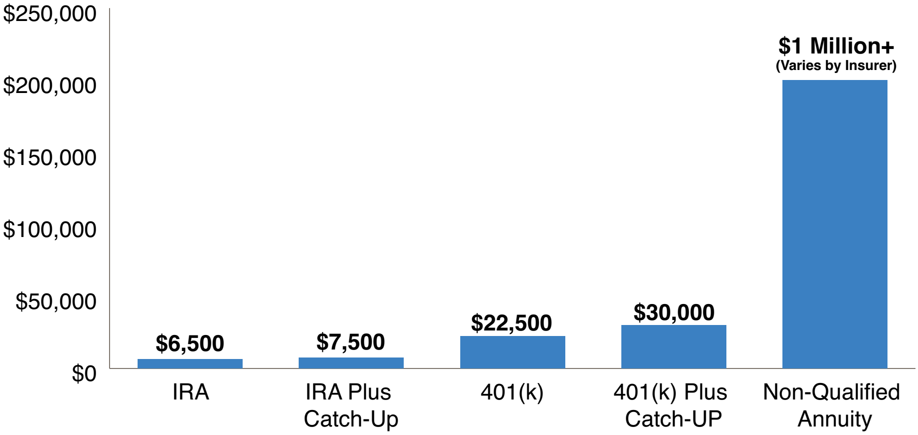
Figure 4-2 Qualified and Non-Qualified Annuities

	Qualified	Non-Qualified
Variable	• Purchased through retirement plans or IRAs using pre-tax dollars, up to specified limits. • The contract value or income payments vary based on the investment performance of underlying subaccounts. • Total sales of qualified variable annuities in 2022 were $69.1 billion.	• Purchased by members of the general public using after-tax dollars. • The contract value or income payments vary based on the investment performance of underlying subaccounts. • Total sales of non-qualified variable annuities in 2022 were $29.6 billion.
Fixed	• Purchased through retirement plans or IRAs using pre-tax dollars, up to specified limits. • Guarantees that the contract owner will earn a stated rate of interest during the accumulation phase of a deferred annuity, and receive a defined amount of income on a regular schedule when the contract is annuitized. • Total sales of qualified fixed annuities in 2022 were $111.9 billion.	• Purchased by members of the general public using after-tax dollars. • Guarantees that the contract owner will earn a stated rate of interest during the accumulation phase of a deferred annuity, and receive a defined amount of income on a regular schedule when the contract is annuitized. • Total sales of non-qualified fixed annuities in 2022 were $91.6 billion.
Total	• Total sales of qualified annuities in 2022 were $181.0 billion.	• Total sales of non-qualified annuities in 2022 were $121.2 billion.

Source: Morningstar, Inc.; Beacon Research

Annuities used within qualified plans are subject to annual contribution limits (Figure 4-3 shows the limits for 2023). The government does not, however, limit the total annual amount of premium payments to non-qualified annuities. Insurance companies may impose maximum premium limits that are typically very high and do not affect most contract owners. Because of this feature, many people view non-qualified annuities as valuable personal retirement accounts to which they can contribute as much as they need for retirement.

Figure 4-3 Retirement Savings Plan Contribution Limits – 2023



Source: Internal Revenue Service – *Publication 590, Individual Retirement Arrangements*

Are Annuities Sold Outside of the Retail Market?

In addition to the annuities described above that are sold through the retail market, several annuities are sold through institutional or private markets. This includes group annuities as well as lesser-utilized annuity products such as private annuities, private placement annuities, and charitable gift annuities. While most of the remainder of the IRI Retirement Fact Book concentrates on individually sold annuities, a brief mention of these additional types of annuities is included for informational purposes.

Group Annuities

Group annuities are typically used as a retirement income plan for employees. Unlike annuities sold in the retail market, group annuity contracts are generally owned by the employer, and employees are participants. Certain individual annuities used in 403(b) plans may also be referred to as "group annuities," but these are actually individually owned contracts purchased in a group setting and contributed to via payroll deduction, for example in the case of a retirement plan for employees of a university or hospital. Group annuities are covered in more detail in Chapter 12: *Tax-Qualified Retirement Plans*.

Private Annuities

In the United States, all commercial annuities are issued exclusively by insurance companies. A "private" annuity is not issued by an insurance company. Rather, it involves the transfer of property (such as real estate) from an individual or a revocable living trust in exchange for an unsecured promise by the transferee (an individual or a non-insurance entity, such as a trust) to make a periodic stream of fixed payments. The tax treatment of private annuities is complex and differs from the tax treatment of commercial annuities.

Private Placement Annuities

Private placement annuities are variable annuity contracts that are not registered under federal or state securities laws. They are available exclusively to investors who meet certain minimum net worth and income levels under such laws. The types of investment options available under private placement annuity contracts often include hedge funds, commodities, managed accounts, and other kinds of private equity offerings.

Charitable Gift Annuities

With a charitable gift annuity, a donor transfers cash or property (including appreciated property) to a charitable organization in exchange for income payments for life or joint lives, with no guarantee period. The federal tax law imposes specific requirements on the relationship of the amount donated and the value of the promised annuity stream. The charity can fund its payment obligations using its own assets, or it can fund them by purchasing a commercial annuity.

What Fees and Expenses Are Associated With Annuities?

What Fees and Expenses are Associated with Fixed Annuities?

A fixed annuity typically does not impose direct expense charges on the contract owner, other than surrender charges (charges for cancellation of the contract during its early years) for deferred fixed annuities. The spread, or difference between what the issuing company expects to earn and what it commits to pay out is intended to cover the insurer's expenses.

What Fees and Expenses are Associated with Variable Annuities?

A variable annuity, on the other hand, involves direct expenses in the form of insurance charges and indirect expenses in the form of management and other fees and expenses associated with the underlying mutual funds in which the variable annuity subaccounts invest.

Insurance, Administrative, and Distribution Charges

The fees and charges commonly associated with variable annuities include mortality and expense risk charges (M&E fees), administrative charges, and distribution charges.

In most contracts, the M&E fee pays for three important insurance guarantees:

- The ability to choose a payout option that provides an income that cannot be outlived at rates set forth in the contract at the time of purchase
- When available, a death benefit to protect beneficiaries
- The promise that the annual insurance charges will not increase

The administrative and distribution charges pay for all of the services involved in the maintenance of variable annuity contracts, such as the preparation of contract statements and mailings and other customer services. Some variable annuities also impose an annual contract fee that is similar to the annual account maintenance fee imposed by many IRAs. This fee generally ranges between $30 and $40 per year. Most insurers waive this fee for contracts with an accumulation or contract value of at least a certain amount, e.g. $25,000.

Mutual Fund Fees and Expenses

Underlying mutual funds incur investment management fees and operating expenses, and in many cases, distribution charges known as “12b-1 fees,” which are named after the SEC rule that governs them. Investment management fees for the mutual funds that underlie the subaccount investment options in variable annuities are, on average, lower than those charged for publicly offered mutual funds. These lower fees have the effect of offsetting, to some extent, the insurance charges. See Chapter 9: Focus on Accumulation with Income Flexibility, for illustrations show how projected accumulation values can vary between variable annuity and mutual fund portfolios.

Surrender Fees

If a contract owner decides to cancel a deferred annuity during the early years of the contract, surrender charges may apply. These charges, if applicable, generally begin in a range from 5 percent to 7 percent of the amount invested and decline to zero over a period of time, such as five to seven years. Surrender charges are structured differently for different annuity products. (See the following section, How Are Variable Annuity Sales Charges Structured?)

Unbundled Fees

Some variable annuity contracts permit purchasers to select from a menu of optional product features, each of which usually has an associated charge. This unbundling approach gives customers the ability to select and pay for only those features they want. Optional features, referred to as riders, include, for example, enhanced guaranteed death benefits and guaranteed minimum living benefits. These riders typically have a separate, additional fee. See Chapter 8: Planning for Future Income, for data on these optional contract rider fees.

Premium Tax

States may impose premium taxes on variable annuity purchases. Currently California, Maine, Nevada, South Dakota, West Virginia, and Wyoming tax life insurance and annuity premiums, and only California and West Virginia tax qualified purchases. Tax rates range from 0.5 percent (California on qualified monies) to 3.5 percent (Nevada on non-qualified). Florida assesses a 1 percent tax on both qualified and non-qualified monies, but it is typically absorbed by the issuing insurance company.

How Are Variable Annuity Sales Charges Structured?

B-Share Variable Annuities

Most variable annuity contracts are B-share products. They are offered with no initial sales charge, but cancellation of the contract during its early years may trigger a withdrawal charge known as a surrender charge. These charges typically range from 5 percent to 7 percent of premium in the first policy year, and subsequently decline to zero, generally after five to seven years (known as the surrender charge period). Some annuity contracts impose surrender charges only during the initial surrender charge period that begins after the contract is purchased, while others associate a new surrender charge period with each subsequent premium payment.

Surrender charges underscore the long-term nature of the annuity product. As long as contract owners remain committed to accumulating money for retirement through their variable annuity, they generally will not incur these charges. In addition to surrender charges, B-share contracts have annual M&E and administration fees. B-shares accounted for over 80 percent of variable annuity sales in 2022.

A number of insurers have begun to offer other types of charge structures to meet different investor needs. The following are the most common.

A-Share Variable Annuities

Like A-share mutual funds, A-share variable annuities have up-front sales charges instead of surrender charges. Sales charges are calculated as a percentage of each premium payment.

A-share variable annuities offer breakpoint pricing, which means up-front sales charges decrease depending on the cumulative amount of purchase payments that have been made. In addition, assets that a contract owner has in other products in the company's product line may be recognized in the cumulative payment amount used to determine the breakpoint pricing. A-share contracts often have lower ongoing M&E annual fees than annuities with surrender charges. A-shares accounted for less than one percent of total VA sales in 2022.

C-Share or No-Surrender-Charge Variable Annuities

C-share, or no-surrender-charge variable annuities, offer full liquidity to owners at any time, without any up-front or surrender charges (although tax penalties may apply to withdrawals before age 59½). There are, however, ongoing M&E and administrative fees. C-shares made up about two percent of total VA sales in 2022.

I-share or Fee-Based Variable Annuities

I-share, or fee-based variable annuities, are intended for investors who favor paying one fee to have their investment portfolio managed by a registered investment advisor or fee-only advisor, (for example, a wrap-fee advisory program). Typically, the sale of an I-share does not result in a sales commission for an advisor from the issuing insurance company. However, the advisor assesses fees for the services, including the I-share contract, which is agreed upon by the client. Consequently, M&E annual fees are generally less than other share-classes due to the absence of commissions. I-shares have no surrender charges and may provide optional living benefit guarantees for an additional fee. I-share sales are a larger percentage of the VA market than they were several years ago; sales of I-shares have grown as overall VA sales have dropped, so I-shares are about eight percent of the VA market today versus three percent 10 years ago.

L-Share Variable Annuities

L-share variable annuities have no up-front sales charges. They typically have relatively short surrender charge periods, such as three or four years, but may have higher ongoing M&E and administrative charges than other share classes. It is becoming more common for L-shares to be structured as a B-share with an optional "buy down," which reduces the duration of surrender charges for an additional fee. This "liquidity rider" expires when the shortened surrender charge period is over, as does its fee. L-shares once accounted for almost one-third of the market but have almost disappeared from the VA landscape due to suitability concerns and represented less than 1 percent of total VA sales in 2022, with almost all this likely coming from additional purchase payments to existing contracts rather than new sales.

O-share Variable Annuities

O-shares are intended to merge the advantageous M&E and surrender charges of A-share and B-share variable annuities, respectively. Unlike A-shares, O-shares do not impose up-front sales charges, while, typically, possessing surrender charge periods akin to B-shares. Instead, M&E charges are assessed against both the account value and the premium, with the premium-based charges progressively declining throughout the surrender period, and ending after the surrender period. These features result in expenses similar to an A-share once the contract is free of surrender charges. The design of O-shares encourages investors to think of variable annuities as a long-term investment by rewarding longer holding periods with lower fees. O-shares were less than three percent of sales in 2022.

X-Share (Bonus) Variable Annuities

X-Share variable annuity contracts credit an additional amount or bonus to the contract value, which is calculated as a percentage of purchase payments added to the contract at or subsequent to contract issue. Bonus amounts generally range from 1 percent to 6 percent. For example, with a 3 percent bonus feature, a contract owner paying $10,000 in premiums would have $300 credited immediately to the balance. This category does not include contracts that credit additional amounts to the contract value after a designated period, sometimes referred to as “persistency bonuses.” Variable annuities with bonus credits may have higher ongoing expense charges and longer surrender periods than variable annuities without bonus credits. Some contracts allow the insurer to re-capture all or part of the bonus if the contract is surrendered within the first few years. Bonus contracts are difficult for companies to offer in a low interest rate environment, and there are far fewer available than there once were. There are only a few X-shares available for new purchase, and the class accounted for about one percent of total sales in 2022; as with L-shares, most if not all of these sales represent additional premiums paid into older X-share variable annuities.

What Are Guaranteed Minimum Death Benefits?

If a contract owner dies in the accumulation phase, a deferred annuity contract will, at a minimum, pay the accumulation value to a named beneficiary. Sometimes the contract may be continued by the beneficiary, with the beneficiary as the new owner. The contractual payout of this benefit varies by policy and can be payable as a lump-sum payment or as periodic annuity payments. (Fees associated with death benefits are discussed in Chapter 8: Planning for Future Income. The tax treatment of death benefits is discussed in Chapter 14: *Regulation and Taxation of Annuities.*)

Most, but not all, variable annuity contracts provide a standard Guaranteed Minimum Death Benefit (GMDB) during the accumulation period equal to the greater of (a) the contract value at death or (b) premium payments minus any prior withdrawals. The “return of premium” (ROP) GMDB gives contract owners the confidence to invest in the stock market, important in keeping up with market inflation, as well as the security of knowing their families will be protected against financial loss in the event death occurs as a time when the account value has incurred losses due to negative market returns.

The value and importance of the death benefit is periodically highlighted during major market corrections, such as the COVID-19 precipitated selloff in equity markets in March 2020; the financial crisis in 2008; or the technology stock led market downturn between 2001 and 2003. While markets inevitably recover and historically go on to reach new highs (as they certainly did in 2021!), the beneficiaries of variable annuity contracts owned by those who die during or immediately after a huge selloff are protected. During each of these major market corrections, variable annuity beneficiaries received death benefits worth significantly more than the value of the annuities, protecting annuity value for beneficiaries. For a VA contract owner dying in a "trough" of financial market returns, the preservation of assets for heirs afforded by a GMDB, even a standard ROP, can be quite significant: estimates of unhedged GMDB exposure at the height of the 2008-2009 financial crisis were as high as $15 billion, meaning $15 billion of death benefit liability in excess of variable annuity account value. A similar circumstance occurred at the onset of the pandemic; contract owners who died in the early months when the market dropped precipitously before recovering were protected from those losses. Beyond ROP there are also several types of enhanced GMDBs that provide additional growth and/or protection of account value. The different types of enhanced GMDBs are described below, some of which have additional associated charges.

Contract Anniversary Value or Ratchet

Some life insurance companies offer death benefits that step up or increase based on pre-determined criteria. Called contract anniversary value or ratchet, these enhanced GMDBs are equal to the greater of (a) the contract value at death, (b) premium payments minus prior withdrawals, or (c) the contract value on a specified prior date. The specified date could be a prior contract anniversary date, such as the date at the end of every seven-year period, every anniversary date, or even more often. A ratchet GMDB locks in the contract's gains on each of the dates specified.

Initial Purchase Payment With Interest or Rising Floor

Some insurers offer a rising floor GMDB that is equal to the greater of (a) the contract value at death or (b) premium payments minus prior withdrawals, increased annually at a specified rate of interest. In some cases, a ratchet and a rising floor may be available within the same contract. Some contracts offer a choice of a ratchet or a rising floor. Though they have become less common and more expensive in recent years due to low interest rates, they are still available.

Enhanced Earnings Benefits

Not all variable annuity death benefits are associated with protection against falling markets. Many variable annuity contracts offer enhanced earnings benefits (EEB) that provide a separate death benefit to help offset federal and state income taxes payable upon death on any gains in the contract. With this feature, beneficiaries receive not only the base death benefit amount, but also an additional amount that is usually equal to a percentage of the contract's earnings at death, e.g., 40 percent.

What Are the Different Types of Guaranteed Minimum Living Benefits?

Prior to 1997, principal protection under variable annuity contracts was offered only in the case of death. In 1997 the first Guaranteed Minimum Income benefit was issued by Equitable, which offered contract holders the opportunity to generate annuity income from the greater of the account value or a guaranteed minimum amount based on the premium, after a multi-year waiting period. In subsequent years insurers developed other "living protection" against investment and/or longevity risk in variable annuity contracts by guaranteeing minimum accumulation values or withdrawal amounts. Some type of living benefit rider is offered on about two-thirds of "open" (i.e., available for new purchases) variable annuity contracts.

Various types of guaranteed minimum living benefit (GMLB) riders are described below. Besides offering these in new contracts, some companies allow them to be added to existing contracts. Guaranteed living benefits are usually offered as riders to variable annuity contracts for an optional charge. (Fees associated with guaranteed living benefits are discussed in Chapter 8: *Planning for Future Income.*)

Guaranteed Minimum Income Benefit

A guaranteed minimum income benefit (GMIB) rider is designed to provide the investor with a base amount of lifetime income when they retire regardless of how the investments have performed. It guarantees that if the owner decides to annuitize the contract (for life, life plus a certain period, or the lives of two people), payments are based on the greater of the contract value, or the amount invested credited with simple or compound "interest" at a rate of 1 percent to 3 percent. The "interest" creates a notional balance upon which annuity payments can be calculated; it does not represent account or cash value. An investor must annuitize to receive this benefit and there is typically a 10-year holding period before it can be exercised. Age limits may also apply.

Guaranteed Minimum Accumulation Benefit

A guaranteed minimum accumulation benefit (GMAB) rider guarantees that an owner's contract value will be at least equal to a certain minimum percentage (usually 100 percent) of the amount invested after a specified number of years (typically 10 years), regardless of actual investment performance.

Guaranteed Minimum Withdrawal Benefit

First introduced in 2002 by The Hartford, a guaranteed minimum withdrawal benefit (GMWB) rider guarantees that a certain percentage (usually 4 percent to 6 percent) of the amount invested can be withdrawn annually until the entire amount is recovered, regardless of market performance. Reducing withdrawals in one year generally does not allow for increased withdrawals in subsequent years. However, if a contract owner defers withdrawals and the account value grows and is "locked in" at certain points as the new "benefit base," the subsequent withdrawal amounts allowed may be larger.

If the underlying investments perform well, there will be an excess amount in the policy at the end of the withdrawal period. If they perform poorly and the account value is depleted before the end of the withdrawal period, the investor can continue to make withdrawals until the full amount of the original investment is recovered.

If the investor decides to terminate the contract before the end of the withdrawal period, he or she will receive the cash surrender value of the contract.

Guaranteed Lifetime Withdrawal Benefit

Another type of GMWB rider that guarantees withdrawals for life was introduced in 2004. The guaranteed lifetime withdrawal benefit (GLWB) guarantees that a certain percentage (typically 3 percent to 5 percent, often based on age) of the amount invested can be withdrawn each year for as long as the contract holder lives. This percentage may vary depending on the person's age when withdrawals begin, whether the payment is guaranteed to continue for the life of one (single life) or two (joint life) individuals, and in some of the newest structures based on the level of an external benchmark such as the 10-year Treasury Constant Maturity Rate. More recently issued benefits may also include other levers that help the insurance company manage the risk of guaranteeing lifetime income on a variable annuity, such as a reduction in the withdrawal percentage rate if the account value is exhausted while income payments are still being made.

In many GMLBs, “step-up” features periodically, e.g., annually or every five years, lock in higher guaranteed withdrawals if investments do well. “Roll-up” features, conversely, increase the amount that may be withdrawn (by increasing the “benefit base” used to calculate withdrawals) during the deferral period, i.e., prior to the commencement of withdrawals. Allocation to a balanced or volatility managed fund, adherence to an asset allocation program, or a minimum allocation to a fixed or fixed income subaccount is often required when electing a GMLB. The liability risk to the insurer may also be managed through dynamic rebalancing, which shifts allocation toward more conservative investment options when equity returns are negative and/or market volatility increases.

In-Plan Lifetime Income Benefit

The standalone lifetime income benefit (SALB) was introduced in 2008. While the SALB did not get much traction in the individual market, the framework has evolved into a defined contribution plan option that embeds a lifetime income benefit into a target-date fund. Since this is not an annuity per se, under current law it is eligible as a Qualified Default Investment Alternative (QDIA), which participants can be auto-enrolled in with the option to opt out if they so choose. This provides in-plan income protection similar to that provided by GLWB on an individually purchases annuity, enabling retirement savers to create their own pensions within workplace plans. Combined with the SECURE Act and SECURE 2.0, which helped alleviate fiduciary concerns by providing a safe harbor for plan sponsors, strong growth is expected in this area in the coming years (see Chapter 14: Regulation and Taxation of Annuities, for more information about the SECURE Act).

Long-Term Care Protection

Some annuity contracts have features designed to address aging Americans’ concerns about long-term care (LTC). Many contracts permit owners to withdraw money from their contracts for long-term care needs without incurring surrender charges. Surrender charges may be waived if, for example, a contract owner has been confined to a nursing home for a minimum period or has suffered a critical illness. Some variable annuity contracts provide GLWB features that double the income payment during a qualified long-term care event, for example admission to a long-term care facility or the inability to perform the Activities of Daily Living (ADLs). Additional benefits may also be offered, such as eldercare resources, referral and consultation services, and discounted long-term care services from a specified group of providers. Hybrid annuity/long-term care products can provide valuable protection against the impact of long-term costs to consumers for whom traditional long-term care may be unaffordable, or unobtainable due to pre-existing conditions.

With the enactment of the Pension Protection Act of 2006, new hybrid products that combine annuities with LTC were introduced. Beginning in 2010, tax-free distribution status was given to both annuity assets and LTC rider benefits used for a qualified LTC purpose. Under prior law, withdrawals taken from the annuity to pay the LTC premiums were taxable and subject to a 10 percent penalty prior to age 59½.

How Is the Value of a Deferred Annuity Determined?

The accumulation period begins when the initial purchase (or premium) payment is made by the contract owner and the contract is issued by the life insurance company. Gifts, an inheritance, or any other source of income can be used to initiate or add to a contract. Typically, insurance companies have minimum requirements for initial and additional premium amounts. However, sometimes a life insurance company will permit a smaller minimum initial payment, for example,

$1,000, if the purchaser agrees to pay premiums on a regular basis, e.g., through automatic payroll deduction. Insurers may also have lower minimum premium requirements for annuities in qualified retirement plans such as 403(b) or 401(k) plans. As is true for all qualified plans, contributions to annuities used to fund qualified plans must come from earned income.

How Is the Value of a Variable Annuity Measured?

The value of a contract owner's variable annuity is equal to the sum of the contract owner's account values in all the variable investment options or subaccounts plus the value of any amounts allocated to available fixed account options, if any.

Unit Values

Each subaccount has a unit value, which is similar to the net asset value (NAV) of a mutual fund. The unit value measures the numerical worth of the assets in a subaccount, per unit of the subaccount owned. The unit value increases or decreases, respectively, with the positive or negative investment performance of the underlying mutual fund in which the subaccount invests and is reduced by insurance charges and the fees and expenses of the underlying mutual fund. Unit values vary among the subaccount options inside a variable annuity. A contract owner's account value allocated to a particular subaccount is equal to the number of units of the subaccount owned multiplied by the current unit value.

Unit values apply to variable annuities in both the accumulation phase and the payout phase. Although the specific unit values differ between the accumulation and payout phases, the concept is the same. During the payout phase, contract owners are entitled to receive a determined number of units of benefit, which translate into an income payment amount based on the unit value at the time of payment. The unit value and resultant income payment may increase or decrease due to investment performance.

Variable Investment Options

Variable annuities offer investment choices called subaccounts, a selection of funds similar to publicly sold mutual funds, often managed by the same fund managers (most variable annuities also offer a fixed account, effectively an embedded fixed annuity, within the variable contract). The value of the subaccounts will fluctuate over time, and the variable annuity's return will be based on the investment performance of those subaccounts.

A variable annuity contract will generally permit the owner to choose from a range of subaccounts with different asset classes and strategies. The choices may include equity funds, bond funds, balanced funds, money market funds, and specialty funds such as international and sector funds.

The subaccounts are often managed by a variety of investment advisors, who may or may not be affiliated with the insurance company. Most of the largest mutual fund companies, and many smaller shops, offer subaccounts that serve as investment options or provide professional fund management services for variable annuities.

Variable Annuity Portfolio Allocation

Variable annuities offer investors a wide variety of funds to choose from to match their risk tolerance and views of the market. There are different types of asset allocation programs available to help variable annuity purchasers analyze their risk tolerance and decide on a specific mix of funds. Choosing the right mix can be a complex process.

Portfolio Rebalancing

Once a contract owner has decided on the investment mix best suited for his or her needs, premium payments are allocated in accordance with those percentages. However, as time goes by, market performance may alter the percentage of the variable annuity's contract value held in certain subaccounts (e.g., equity exposure may be significantly higher after a period of strong stock market returns). Many variable annuity issuers offer programs that automatically maintain a pre-determined investment diversification based on the specific needs of each investor. These programs, referred to as portfolio rebalancing programs, periodically reallocate variable annuity contract assets among fixed and variable investment options to reflect the proportions originally selected.

Dollar Cost Averaging

Contract owners who are wary of investing when the market is at a peak can take advantage of dollar cost averaging programs offered under many variable annuity contracts. An owner may choose to allocate a substantial portion of his or her premium payments to a particular stock fund. If the allocation is made all at once, it is possible that a single purchase price could be locked in when asset values of the stock fund are relatively high. With dollar cost averaging, the premium is systematically transferred (typically from the variable annuity's fixed account option or a money market option) to one or more stock, bond, or balanced funds over a specified period of time, with the goal of investing at lower, as well as higher, prices. While dollar cost averaging does not ensure a profit or protect against a loss, it can be an effective investment technique.

Importance of Tax Deferral to Portfolio Allocation

The benefits of tax deferral are vital to rebalancing programs and dollar cost averaging. In a taxable account, such as a stand-alone mutual fund, each time an investor sells a stock, mutual fund, or other investment, and replaces it with another in order to reallocate assets, the investor can be required to pay short- or long-term capital gains tax on any investment growth. With a variable annuity, an owner can rebalance between funds as desired without being taxed, thereby maximizing investment potential.

Transfers

While variable annuity contract owners may transfer money, tax free, from one investment option to another during the accumulation period, certain restrictions typically apply. Owners may be restricted to the number and amount of transfer payments allowed in any given year from a fixed account contained inside a variable annuity contract. Another restriction may also limit the number of transfers made among the variable investment options within a specified period of time. Transfers in excess of such limits may be subject to nominal administration charges or alternative transfer request methods, such as a requirement to send such requests via U.S. Mail versus online or telephonic instruction.

How Is the Value of a Fixed Annuity Measured?

Fixed annuities offer a rate of return that is determined by the insurance company for a set period of time, subject to a specified minimum. When the applicable period is over, the company may offer a new rate for the next period, which can be for a different length of time. Fixed annuities generally specify a minimum credited interest rate for the lifetime of the contract.

There are several types of deferred fixed annuities available, each with its own method of crediting interest.

- *Book value deferred* products earn a fixed rate for a guaranteed period. The surrender value is based on the annuity's purchase value plus credited interest, net of any charges.
- *Market value adjusted* (MVA) annuities are similar to book value deferred annuities, but the surrender value is subject to a market value adjustment based on interest rate changes.
- *Fixed indexed annuities* (FIA) guarantee that a certain rate of interest will be credited to premiums paid but also provide additional credited amounts based on the performance of a specified market index (such as the S&P 500).

Individual fixed indexed annuity contracts have additional interest crediting provisions. These include:

- *Crediting method* — the method used to measure the change in the underlying index, e.g., point-to-point or annual reset.
- *Participation rate* — the percentage of the calculated index gain credited to the contract owner as interest. This can be guaranteed or eligible for reset.
- *Spread/Margin* — the percentage by which the gross index gain is reduced before being credited to the contract owner as interest.
- *Cap* — the maximum index-based interest credited to the contract owner. This can be guaranteed or eligible for reset.
- *Volatility Controlled Indexes* — custom indexes intended to mute the effect of ups and downs in the markets they track; may be used instead of, or in conjunction with, participation rates, caps, and spreads.

What Happens to the Annuity Value if the Contract is Surrendered?

Deferred annuity contracts permit the contract owner to surrender the annuity contract during the accumulation period and receive a cash payment from the insurance company. This amount is called the cash value or cash surrender value of the contract. It equals the sum of premiums paid plus any earnings, minus prior withdrawals and charges deducted. The owner may take partial withdrawals or fully surrender the contract during the accumulation phase. Penalties for early withdrawal may be incurred and federal income taxes will apply to any gain in the contract value. The amount paid to the contract owner on surrender may be subject to surrender charges, which generally range from 5 percent to 7 percent. Some deferred annuity contracts impose surrender charges only for an initial period after the contract is purchased; others start a new surrender charge period for each individual premium paid. Surrender charges usually decline to zero over a period of time, such as five or seven years.

A partial surrender is the withdrawal of an amount less than the entire cash surrender value of the contract. Partial surrenders can also be taken as a pre-scheduled series of payments under a systematic withdrawal plan. Many contracts permit annual withdrawals of an amount, such as 10 percent of the contract value, free of a surrender charge. Tax penalties may apply, however, in the event such withdrawals occur prior to the contract owner reaching age 59½.

How Are Annuities Used to Generate Retirement Income?

While much of the focus on annuities in recent years has been on their value as a savings vehicle for retirement, their value as a source of lifetime income during retirement is equally important. Traditional sources of guaranteed retirement income are diminishing at the same time retirees are living longer, more active lives. This places the burden on individuals to both carefully save for retirement and wisely manage their investments during retirement, so their money lasts as long as they live. How retirees decide to receive income from their annuities once they retire can play an important role in achieving this outcome.

What Are the Various Options for Receiving Retirement Income?

Once a person is ready to retire, annuities offer a number of retirement income options. The contract owner can choose to receive all the assets from the annuity at once, opt for a series of withdrawals of his or her choosing until all the assets are exhausted, or decide to exercise the annuitization features of the contract.

The following information pertains to non-qualified annuities that are purchased with after-tax dollars. While the payout options available are the same for annuities purchased as part of qualified retirement plans, as discussed in the last section of this chapter the tax consequences are different.

Lump-Sum Option

When a contract owner elects a lump-sum distribution, the annuity is surrendered and all assets are withdrawn from the contract. Taxes will be due on earnings in the year the money is received, and tax penalties may apply to withdrawals before age 59½. With this option, individuals are still faced with the need to generate a guaranteed stream of income.

Systematic Withdrawal Plan

With a systematic withdrawal plan, the assets are left in the annuity and the contract owner receives distributions at regular intervals until the assets have been exhausted or the contract owner elects to suspend the operation of the plan. All earnings on the investment are considered to be distributed before any return of principal and are taxable at ordinary income tax rates. Assets remaining in the annuity continue to grow tax deferred until withdrawn.

The principal advantages of a systematic withdrawal plan are the flexibility provided to the contract owner and the ability to maintain full ownership of the assets. The principal disadvantage is that the contract owner retains the risks associated with both uncertain longevity and investment fluctuations, particularly the exposure to adverse market performance during the early stages of retirement.

If a specified dollar amount is withdrawn each period, whether adjusted for inflation or not, the contract owner assumes the full risk of market cycles. The very principles that recommend dollar cost averaging as a successful strategy for entering the market work against the contract owner in a liquidation strategy. Withdrawal of a fixed dollar amount means that a higher percentage of assets will be liquidated in a down market than in an up market. This can be a very dangerous strategy, even if long-term investment performance meets anticipated targets, since the withdrawal of assets in earlier years can prevent the overall portfolio from achieving the projected return.

The withdrawal of a specified percentage of assets rather than a specified dollar amount may help reduce this risk. Many people plan their retirement income based on an average rate of return on their investments (such as 8 percent). If they happen to retire during a time of far lower (or even negative) returns, however, the specified percentage of assets they withdraw may not provide sufficient income to maintain their desired lifestyle. To help reduce the impact of market fluctuations on retirement income, it is important for retirees to have a variety of diversified investments in their portfolios, including annuities, which can help create a guaranteed source of income that will last as long as they live.

Guaranteed Withdrawals

Contract owners electing a guaranteed minimum withdrawal benefit (GMWB) rider can choose to receive the value of their investment through annual withdrawals (up to a set percentage) at least until the entire amount invested is completely recovered. Contract owners electing a guaranteed lifetime withdrawal benefit (GLWB) can choose to withdraw a percentage of their contract value each year for as long as they live, even if the account value is exhausted. Distributions are deemed to represent investment earnings until total payments equal the account value in excess of total purchase payments and are taxable at ordinary income tax rates, after which time payments are deemed return of principal and are not taxed. Payments made by the insurance company after the account value is reduced to zero are deemed ordinary income and taxed as such.

Contract owners electing these benefits have greater control over their assets but may receive lower monthly payments than if they annuitize. While some GLWBs are beginning to tailor the percentage withdrawal to the age of the contract owner, it is only through annuitization that an investor can maximize the benefit of mortality risk pooling.

Annuitization

Annuitization involves turning the contract owner's accumulated assets into a stream of income based on the amount of the contract, the annuitant's age, payout choices, etc. The insurance company guarantees that it will provide payments for the life of the annuitant(s). With a deferred annuity, money is saved and invested during the accumulation period, and then annuity payments are received during the income period (e.g., during retirement). With an immediate annuity, payments begin immediately or within one year after the annuity is purchased. Payments can be either fixed or variable and guaranteed for one person's life, for the lives of two people, and/or for a specified period. Payments may also be structured with a cash refund feature, which provides for a payment to beneficiaries of an amount equal to the difference between the annuitized amount and the total payments made prior to the annuitant's death, should death occur before payments at least equal the amount annuitized.

Deferred Income Annuities

With a deferred income annuity (sometimes called longevity insurance), a retiree can purchase a contract at one point in time, for example, at age 65, but defer payments until a later time, for example, at age 85. Individuals not living until the commencement age will not receive benefits;

and individuals who do live to the required age and beyond, will receive income payments. Because these products usually have no death or living benefits, and not all contract owners will live long enough to collect income, insurance companies can maximize insurance leveraging (risk pooling) and thus make larger income payments to retirees still living. Recent innovations include optional death benefit and joint and survivor payments, but the trade-off is a higher premium or smaller monthly payments. The issuance of new regulations from the U.S. Treasury in June 2014, the "Qualified Longevity Insurance Contract" rules, provided clarity around the use of these products in qualified plans by establishing a deferred income annuity purchase amount limit of the greater of 25 percent of account value or $125,000 and created provisions for the addition of a death benefit and the ability to reverse an excess purchase payment in order to avoid tax penalties. The SECURE 2.0 Act removed the 25 percent limitation and increased the QLAC purchase limit to $200,000 for 2023.

What Are the Benefits of Annuitization?

By exercising the annuitization option of a deferred annuity (or by purchasing an immediate annuity), the contract owner can transfer the longevity risk to the insurance company and, if a fixed annuity is chosen, the investment risk as well.

As mentioned earlier, annuities are the only financial instruments available today, other than Social Security and pensions, that can guarantee a lifetime stream of income during retirement. Annuitizing a portion of retirement savings provides retirees with an effective hedge against outliving their assets. And because annuity owners are part of a mortality pool, the annuity payments received are larger than they could generate by saving on their own and systematically withdrawing funds in amounts that give them a reasonable assurance of not running out of money.

As part of a comprehensive retirement portfolio, annuities both reduce the risk of running out of money if a person lives a long life and increase the amount of each income payment received.

What Types of Annuity Payout Options Are Typically Available at Annuitization?

One of the first choices contract owners may have to make once they decide to annuitize is whether to receive fixed or variable payments. Owners of deferred fixed annuities can elect only a fixed payout option. Owners of deferred variable annuities, however, can sometimes choose either fixed or variable payouts. Once a selection is made, it is usually irreversible. With fixed payments, the insurance company sets a given amount it will pay (typically monthly) for the term of the contract. With variable payments, the amount of each payment is not guaranteed but changes with the performance of the underlying portfolio selected by the contract owner. Fluctuations in these payments can sometimes be reduced by opting for level payments (which hold payments level for a certain period of time) or stabilization guarantees (which provide a floor below which payments will not fall).

Life Annuities

A life annuity provides an income stream guaranteed to last as long as the annuitant lives. Under a straight or pure life annuity, annuity payments stop when the annuitant dies. A joint and survivor annuity (often selected by spouses) provides income for as long as either of the two annuitants is alive, although the amount of each payment will be less than if the payment were based on a single life. Payments can stay the same or decrease after the death of the first annuitant. Under a joint and two-thirds annuity, each payment made after the death of the first annuitant is two-thirds of the amount paid while both annuitants were alive. This can be an effective strategy, as it results in a higher payment when both annuitants are alive and expenses will likely be lower for one person than for two.

As discussed previously, a valuable feature of an annuity is the fact that it can generate higher income payments than an individual systematic withdrawal plan and continue payments for as long as a person lives. But what about the investor who does not live long enough to receive many payments? There are a number of options for mitigating this risk. Each, however, results in a lower basic periodic payment.

Period Certain Annuities

With a period certain annuity, payments are guaranteed to continue for a specified time, for example, 10 years, no matter how long the annuitant lives. If the annuitant dies before the period has expired, payments continue to the designated beneficiaries for the remainder of the period. Period certain annuity payments typically are available for periods from five to 30 years. This option, however, offers no protection against longevity risk as payments are only made for the fixed period selected.

Life Annuities With a Period Certain

Life annuities with a period certain option guarantee payments for the life of the annuitant, but also guarantee that these payments will continue for a set period of time if the annuitant dies before the period has expired. Payments continue to the designated beneficiaries until the guarantee period has ended.

Cash Refund Annuities

With a pure life annuity, payments stop when the annuitant dies. In the most extreme case, an annuitant could die after one payment is made. Some annuitants prefer to hedge against this possibility by setting up a life annuity with some form of refund feature. As indicated earlier, adding such provisions results in a lower payment than would otherwise be the case.

There are two types of refund annuities now being offered that pay a refund to the beneficiary if the annuitant dies before the total of the annuity payments received equals the premiums paid for the annuity.

- *A cash refund annuity* provides for a lump sum refund of the premium minus the annuity payments already made at the time of the annuitant's death.
- *An installment refund annuity* provides that payments will continue in installments until the amount received is equal to the premiums paid.

Risk Tolerance vs. Longevity

In deciding what type of annuity payment option to choose and how much to commit to it, individuals must determine their risk tolerance with respect to their possible longevity, as well as the relative importance to them of receiving lifetime income versus leaving money to their heirs. All else equal, individuals who live beyond average life expectancy will generally realize higher income but lower estate values when using annuities versus other approaches.

How Are Variable Annuity Payment Amounts Determined?

The amount of each payment received from a fixed annuity is calculated at the time of annuitization and does not change during the life of the contract. The amount of each variable payment, on the other hand, fluctuates based on the investments chosen. Since the investment return of the portfolio cannot be determined in advance, some assumptions must be made in order to calculate the amount of the initial payment under the contract. This is accomplished by selecting an assumed interest rate, or AIR. After the initial payment, each subsequent payment is determined by adjusting the previous payment up or down based on the actual performance of the underlying portfolio for the period of time in question. If the portfolio earns more than the AIR, the subsequent payment will increase. If the portfolio earns less, the payment will decrease. If it earns the same amount, the payment will stay the same.

Some contracts set the AIR, but most allow the contract owner to choose from a range (usually 3 percent to 6 percent), the outside limits of which are set by state regulations. Selecting a low AIR will cause payments to increase faster with higher positive returns, or decline more slowly with low or negative returns, than if a higher AIR were selected. However, the initial income payment will be less than if the higher AIR were selected.

Level Annuity Payments

Some variable annuity contracts provide payment streams that can be adjusted at periodic intervals of up to 12 months, rather than monthly, to provide the annuitant with an element of certainty. This allows the annuitant to plan on a given level of payments for the period in question. When the periodic adjustments are made, however, they are likely to be more substantial than if the adjustments had been calculated more frequently.

Payment Stabilization Guarantees

Other variable annuity contracts offer payments supported by “floors.” These floors guarantee that subsequent payments will never be less than a given percentage of the original payment e.g., 85 percent or 100 percent, regardless of the performance of the underlying portfolio. Some provisions, limit the investment choices underlying the annuity, providing the insurance company with the opportunity to hedge its guarantee with derivative instruments. These floors provide contract owners with a safety net that may make them more comfortable with having their annuity payments subject to the variability of stock market performance. If a contract owner chooses this feature, however, payment amounts will be lower than if no floor were elected.

Liquidity Options

Historically, once an annuity contract was annuitized the stream of payments could not be altered. Some insurance companies now offer life annuities that allow annuitants who have also selected a period certain option to receive an advance of a given percentage of income payments, subject to certain restrictions that vary by company. These partial commutations, as they are called, reduce the remaining annuity payments. Some companies also allow the liquidation of the entire annuity, converting the value of the future stream of income into a lump-sum payment. If this option is exercised, all future payments cease.

How Are Annuity Payments Taxed?

If an annuity (fixed or variable) was purchased with non-qualified or after-tax dollars, a portion of each payment is considered to be a tax-free return of principal. The remainder of the payment is subject to taxation to the extent it represents earnings. Current federal income tax law specifies that the taxable portion of annuitized payments is taxable at ordinary income tax rates.

To determine the amount of each fixed annuity payment that qualifies as a tax-free return of principal, the insurance company makes an underlying calculation based on a formula known as the "exclusion ratio." For variable annuities, since the amount of each future payment is unknown, a different calculation is performed to determine the exclusion amount.

If an annuity was purchased with qualified or pre-tax dollars using funds from a 403(b), a 401(k), or an IRA (other than a Roth or an after-tax IRA), the full amount of each distribution is taxable at ordinary income tax rates, even the amount attributable to principal.

Qualified assets, once they have been annuitized, are not subject to the required minimum distribution rules of the Internal Revenue Code since the insurance company is deemed to have already made the appropriate calculation for a lifetime distribution of the underlying assets. (See Chapter 14: *Regulation and Taxation of Annuities*, for more details on taxation.)

How Are Annuities Used in Estate Planning?

A variable annuity, while not designed as an estate planning tool, does offer some benefits in this area. An annuity avoids probate, provides flexibility when passing on assets to heirs, and can potentially increase the likelihood of leaving a larger estate in some circumstances.

Variable Annuities Avoid Probate — A variable annuity is a contract between an owner and an insurance company. The contract requires that a beneficiary be named. When a contract owner dies, there is a payout directly to the beneficiary. As a result, the annuity assets do not go through the probate process.

Probate, or the distribution of a deceased's assets via the court system, can be costly and time consuming. There are attorney fees, court costs, and administrative expenses, and the process slows the distribution of proceeds. Plus, probate proceedings are a matter of public record. Assets held in a variable annuity bypass this process and go directly to the beneficiary.

Variable annuity proceeds will be subject to probate only if the estate is named as beneficiary, when no beneficiary is named, or when a death benefit is disclaimed by the beneficiary and no contingent beneficiary is named.

The Restricted Beneficiary Option Offers Advantages — Naming a restricted beneficiary is a unique option available to an annuity owner. This enables the owner to direct the amount, frequency, and timing of the distributions. Choosing the restricted beneficiary option provides the added benefit of continued tax-deferral over the life expectancy of the beneficiary. The individuals named as beneficiaries get payouts over a period of time, during which the proceeds grow tax deferred and compound over time, potentially providing many times more from the investment than a lump-sum payout. An individual must be directly named as beneficiary to take advantage of this treatment. It is necessary to complete paperwork instructing the insurer how to distribute the death benefit proceeds.

A Single Premium Immediate Annuity as an Estate-Building Tool — Here is an example of an annuity product that can, under some circumstances, increase the value of an estate. A single premium immediate annuity (SPIA) is usually not considered to be a vehicle that can help preserve or increase the size of an estate. Indeed, many people have the false belief that a SPIA always reduces the size of the estate. However, for those retirees who need to make regular withdrawals from their assets, a portfolio that uses a SPIA is more likely to leave a larger estate than a portfolio without it. Consider an example. Most retirees, especially as they age, place at least half of their money in fixed investments, usually bonds or certificates of deposit. Regular income is often taken from these fixed investments. As of July 2023, the average 10-year High Quality Market (HQM) Corporate Bond Spot Rate was 5.14 percent, about 40 basis points higher than at the same time last year. For a retiree to withdraw $1,000 a month ($12,000 per year) from high quality corporate bonds, that person would have to invest approximately $235,000, versus almost $500,000 before rates began to rise in 2021, illustrating the tremendous impact interest rates have on income streams during retirement. In 10 years, the retiree would still have the $235,000 investment "at par," or the redemption value of the bonds. However, the actual value of the bond holdings would be lower if rates had risen and higher if they had fallen.

However, rising rates benefit retirees using annuities for income as well. A 70-year-old male could elect to receive the same $1,000 monthly income from a SPIA with a 10-year certain period for a premium of about $145,000. Imagine this hypothetical retiree has the same $235,000 to invest for retirement income. He can use $145,000 for the SPIA purchase while investing the remaining $90,000 in a side fund for long-term growth. After 10 years, assuming an annual return from a balanced portfolio of approximately 9.7 percent per year, the side fund would grow to the same $235,000. The side fund also has the potential to grow significantly larger if returns are higher, as would certainly be possible based on the long-term average return of a diversified investment portfolios. Additionally, options such as Registered Index Linked Annuities (RILAs) enable participation in market growth with some protection against potential extreme market loss events discussed earlier. According to the Center for Research in Security Prices, the historic average annual return of a 60 percent stock, 40 percent bond portfolio from 1961 through June 30, 2021 was about 10 percent, which would grow the hypothetical side fund in this example to over $240,000. In addition, the retiree continues receiving the $1,000 monthly payment from the annuity for life, while the bond holder would get no further income after the bonds mature and may have to reinvest the proceeds at a lower interest rate (though the value of the bonds would likely have risen in this scenario, providing a partial offset). A 70-year-old male has an 80 percent chance of living 10 years, a 63 percent chance of living 15 years, and four in 10 70-year-olds can expect to reach at least age 90, which means that most people who buy a SPIA at age 70 will be alive at age 80 and are likely to have more money and more income with a SPIA and a side fund than if they relied solely on bonds for income.

A Variable Annuity Offers a Death Benefit — Most variable annuities offer a death benefit, which guarantees that if the annuity owner dies at a time when the market value is less than the money they put into it because of market declines, the beneficiaries will get the original purchase amount, minus any withdrawals that may have made. In some cases, the beneficiaries can receive more than was invested via an enhanced death benefit, which steps up the death benefit payout based on positive performance of the investments, or a fixed percentage increase annually in the promised death benefit payout. A beneficiary must often recognize income and pay taxes on the earnings portion of the death benefit payout. The earnings enhancement death benefit can help offset a higher tax bill.

Overall, annuities are not designed as estate-planning tools. But these products do help a person protect his or her financial security and can often lead to a larger estate if an annuity is invested in a retirement portfolio.

How Are Annuity Products Developed and Sold?

In the United States, commercial annuities are issued by insurance companies. When new fixed and variable products are developed, they must be filed with the state's insurance department. Before these products can be sold, each state where they will be available must provide written approval.

Because variable annuities are considered securities as well as insurance products, when a new variable annuity is developed, a registration statement must be filed with the Securities and Exchange Commission (SEC). This statement includes a prospectus that discloses, among other things, the fees and charges associated with the annuity contract; a description of the various benefits, rights, and privileges afforded under the contract; any changes that can be made to the contract; and the risks and tax consequences associated with investing in the contract. The prospectus, which is updated annually, is a vital source of information for all contract holders and should be read thoroughly.

Insurance Company Ratings

Annuity guarantees are subject to the claims-paying ability of the issuing insurance company. It is therefore important to consider the financial soundness of a company before making a purchase. Companies are rated by one or more of the following independent industry analysts: AM Best Company, Standard & Poor's, Fitch Ratings, and Moody's Investors Services. The ratings do not apply to the underlying mutual funds, which are subject to market risk and will fluctuate with changes in market conditions. Ratings can differ somewhat among the analysts, so it is useful to check the ratings from at least two analysts.

Who Can Sell Annuities?

People who sell variable annuities need training in both securities and insurance. This training can be obtained from many sources. Some distributors provide in-house training to their registered representatives; others utilize training provided by insurance company wholesalers and independent third-party educators.

Fixed annuity sellers receive much of the same instruction as those selling variable annuities but do not need the securities training.

To legally sell annuities, individuals must first obtain a state insurance license from the state in which their office is located. A non-resident license must be obtained for all states in which out-of-state clients reside.

Since variable annuities are considered securities under federal securities laws, individuals who wish to sell them must, in addition to having an insurance license, be associated with a broker-dealer, be federally registered as a representative, and pass a Series 6 exam, or the more comprehensive Series 7 exam. In some jurisdictions, a state securities license is also required.

Where Can Annuities Be Purchased?

Some insurance companies sell their products only through a dedicated sales force (captive agents); others use agents who represent many companies and have no primary relationship (independent agents). But annuities can also be purchased from a variety of different sources, some of which may sell both fixed and variable annuities while others may market only one type.

Variable annuities can be purchased through several distribution channels, such as independent FINRA firms, wire houses, regional investment firms, captive agents, and banks. Fixed annuities are sold through these same distribution channels, yet sales are dominated by independent agents and banks. The difference in the percent of sales by distribution channel for fixed and variable annuities may be explained, at least in part, by the fact that purchasers of fixed annuities tend to be more conservative with their investments than those who buy variable annuities.

How Are Variable Annuity Commissions Determined?

Broker-dealer firms may be paid a commission by insurance companies when they sell variable annuity contracts. The amount of compensation depends upon the issuing insurer, the relationship the broker-dealer has with the insurer, the types of annuities sold, the amount of money invested in the annuity, and the way commissions are paid. Commissions can be paid in full at the time the annuity is sold, as a level commission over the life of the contract or some other period, or as a smaller amount at the time of the sale with a trail commission paid each year thereafter for a period. Both fixed and variable annuities may also be sold within managed, fee-based accounts, where the account is charged an ongoing annual fee and there is no commission paid on the sale of the annuity.

Registered sales representatives are, in turn, paid a commission when they sell an annuity contract. Commissions paid to representatives are generally less than the full amount paid to the broker-dealer and may or may not be on the same basis. Also, certain management personnel, such as branch managers, may be paid for sales made by representatives over whom they have supervisory responsibility.

In addition to commissions, the broker-dealer may receive other forms of compensation from insurance companies, such as lodging, travel, and meals at insurance company-sponsored meetings. Some broker-dealers also receive monetary and other support to conduct client and educational seminars.

Insurance companies recoup the commissions and other compensation they pay through the various fees, charges, and deductions within the annuity contract, including any sales load that may be imposed, but no one charge is specifically earmarked to pay commissions.

The Retirement Saving and Income Handbook

A Basic Guide to Annuity and Non-Annuity Solutions for Accumulating and Preserving Wealth, and Generating Retirement Income

2023

Insured
Retirement
Institute

Annuities and Other Solutions Included in this Handbook

ANNUITY SOLUTIONS

5 Fixed Annuities

7 Fixed Indexed Annuities

9 Variable Annuities

11 Registered Index-linked Annuities I — Floor Strategy

13 Registered Index-linked Annuities II — Buffer Strategy

16 Living Benefits I — Guaranteed Lifetime Withdrawal Benefits

18 Living Benefits II — Guaranteed Minimum Income Benefits

19 Single Premium Immediate Annuities

NON-ANNUITY SOLUTIONS

6 Certificates of Deposit

8 Fixed Income + Index Call Options

10 Open-end Mutual Funds

12 Managed Floor Exchange-traded Funds (Managed Floor ETFs)

14 Buffered Exchange-traded Funds (Buffered ETFs)

16 Systematic Withdrawal Plans

18 Variable Income Plans

20 Bond/CD Ladders

APPENDIX

21 Definitions of Key Terms

Structure and Content of this Handbook

HOW TO USE THIS HANDBOOK

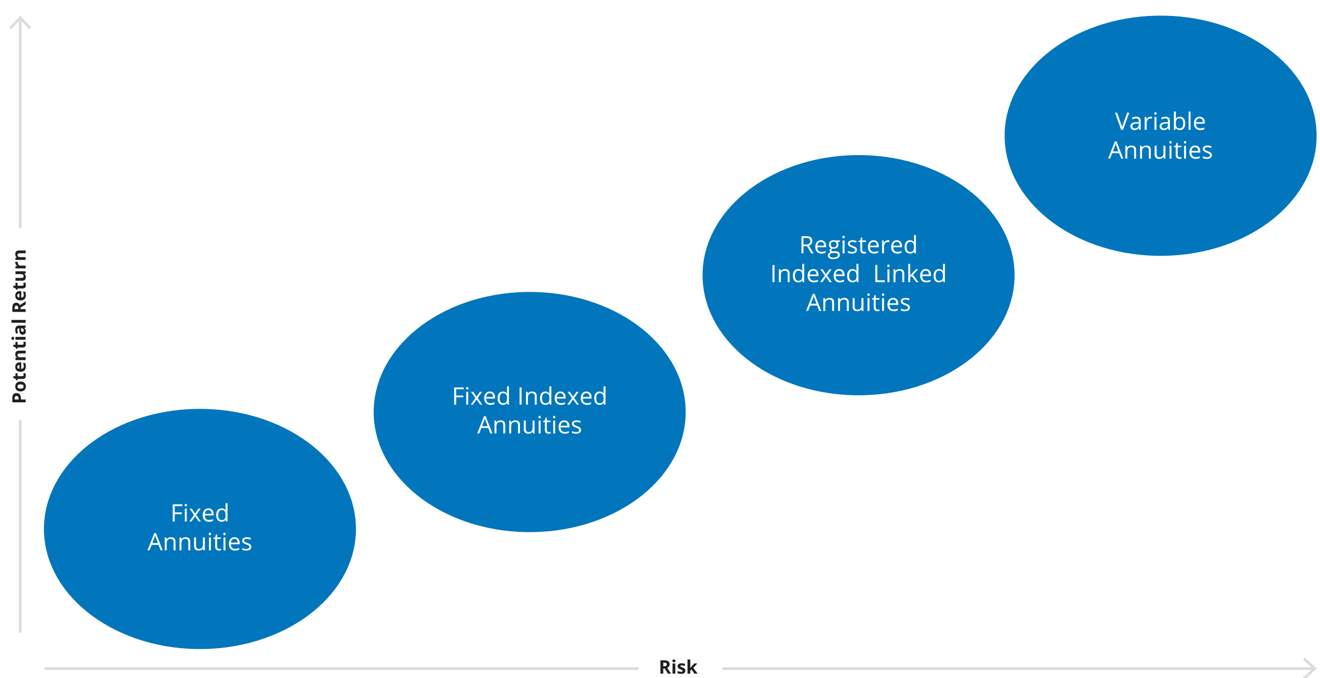
First, a few words on what this handbook is, and what it is not. This is not an exhaustive guide to all annuity and non-annuity products available in the market today, nor does it purport to present all the features and benefits of each product discussed or all the various features and benefits offered by insurers, asset managers, and banks in their unique product offerings. Rather, this handbook provides a basic description of each product or solution, a synopsis of common features found in each, and a visual representation of how each one functions. It is intended as an introduction to annuities and other solutions that provide investors with opportunities to accumulate wealth, fully or partially protect investable assets from market risk and market volatility, and efficiently distribute wealth to create supplemental income throughout retirement.

WHY ANNUITIES?

Annuities play a unique role in an investor's portfolio. While alternatives can be effective and, in some cases, preferable, only annuities guarantee income for the life of the investor, no matter how long that life may be. This guide describes the basics of these products and provides examples for how they can help consumers achieve their financial goals.

RISK VERSUS RETURN

All deferred annuities can be thought of as falling along a spectrum of potential return and market risk. Fixed annuities, which guarantee preservation of principal but credit a fixed rate of interest, have the lowest level of market risk but also the lowest potential return. Variable annuities, conversely, can be fully invested in risk assets (i.e., stocks) through subaccounts that are like open-end mutual funds, and therefore have the highest risk but also the highest potential return. Immediate annuities, in their purest form, solely represent income and are not shown in the chart below.



Benefits Common Across Annuities

Rather than repeat certain benefits common to all or most insured (annuity) products and solutions on each page of this guide, the simple table below briefly describes each benefit and notes exceptions to the description and limitations.

Benefit	Description	Exceptions and Limitations
Tax-deferred interest/ earnings on unlimited after-tax contributions	Federal and state income taxes are not payable until monies are withdrawn from the annuity or the account value is annuitized.	Immediate annuities do not have a deferral period, therefore no tax deferred earnings accrue.
Death benefits	Payments to beneficiaries upon the death of the annuity owner. Enhanced benefits may be available paying an amount greater than the annuity cash value, such as "return of premium" options which guarantee a death benefit of at least the total amount invested.	Annuitized income may not continue after the death of the annuitant or may be limited.
Exemption from probate	Monies paid out to beneficiaries upon the death of an annuity owner are excluded from the probate process.	For trust-owned annuities, the provisions of the trust govern distribution of assets and generally avoid probate.
Protection from creditors	Annuity benefits may be unconditionally exempt from seizure by creditors.	Levels of protection vary by state. AK, CA, FL, GA, HI, IN, TX, and LA provide for 100% annuity protection.
Protection from outliving one's income (annuitization)	All annuities can be "annuitized," i.e., contributions or account balances can be converted into guaranteed lifetime income. In non-qualified contracts, the portion of each payment representing the amount invested is not taxed (this is the "exclusion ratio").	Account values are generally not accessible other than through set, scheduled ongoing income payments. The insurance benefits of annuities are subject to the claims paying ability of the issuing company. State funds exist to help make policy holders whole in the event of insolvency, up to specified dollar amounts which vary by state.

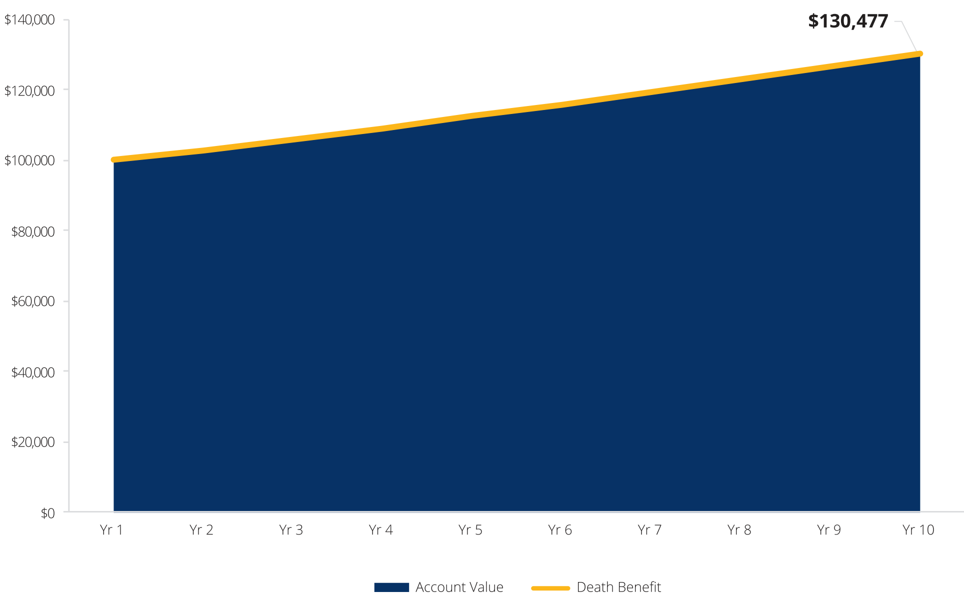
Fixed Annuities

SUMMARY

Fixed annuities are insurance contracts that offer tax-deferred investing and a guaranteed rate of return in the form of interest credited to the contract by the issuing insurance company.

HOW IT WORKS

An initial purchase payment is invested by the contract owner and managed in the insurance company's general account. The insurance company guarantees that the account will earn a specific interest rate for a specified period. This period is known as the accumulation phase. Many fixed annuities have specific terms after which they "mature" and will automatically renew for another term of the same length unless liquidated or exchanged, similar to the manner in which CDs issued by a bank mature. Others continue to credit interest at renewal rates published each year, after an initial guaranteed rate period, until the contract is terminated. As with all deferred annuities, fixed annuities can be "annuitized," or converted into lifetime income payments.



In this example, $100,000 is invested in the annuity and the annuity credits interest at a 3% rate for 10 years, resulting in an ending value of $130,477. The contract owner dies 10 years after the contract is issued and the accumulated value is paid to the beneficiary. Basic fixed annuities are simple and straightforward, often have higher crediting rates than certificates of deposit, and include the benefit of compounding interest on a tax deferred basis.

BENEFITS

- Principal protection and a guaranteed minimum rate of return, subject to the claims paying ability of the issuer.
- Fixed annuities offer beneficiaries a simple standard death benefit: the annuity's accumulation value or the minimum guaranteed surrender value, whichever is greater, which ensures beneficiaries receive no less than the current value. Some products offer optional enhanced death benefits that may pay out a higher value.
- Ability to annuitize the contract to create lifetime income in retirement.
- Interest rates for fixed annuities are usually higher than what you would get from a CD.

RESTRICTIONS AND LIMITATIONS

- Most contracts have a minimum investment amount, commonly $5,000 to $25,000, and a maximum of $1 million without prior approval.
- Annual withdrawals exceeding 10% of the amount invested may be subject to an early withdrawal penalty (surrender charge) during the early contract years (three years is common).
- Most fixed annuities are "spread products" without explicit fees (other than for optional benefits).

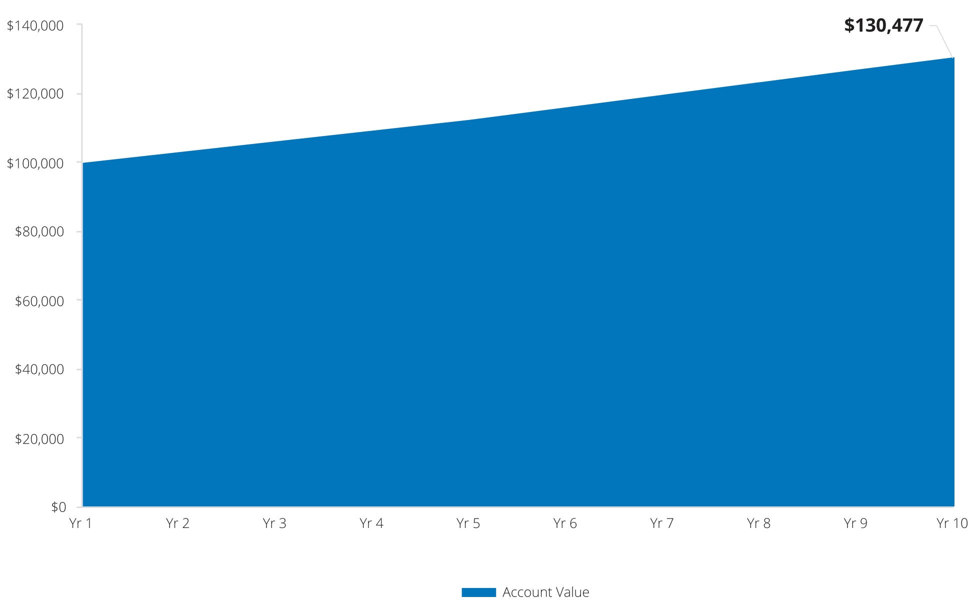
Certificates of Deposit

SUMMARY

Certificates of deposit (CDs) are fixed income investments issued by banks and credit unions. CDs are credited with a fixed rate of interest on a lump sum for a specified number of years. In general, the longer until the CD matures, the higher the interest that is paid. Virtually every bank and credit union offers a variety of CD options.

HOW IT WORKS

An initial contribution is made to purchase the CD, which is then held for the time period specified with interest credited and compounded annually. The interest rate credited to the CD is locked in for the term (e.g., a six-month or one-year CD) and cannot be changed by the bank. When the CD matures at the end of the specified period, it may be liquidated, or cashed in, within a specified time period, usually 30 days. After 30 days the CD will automatically roll over to a new CD for the same time period at prevailing interest rates. Unless held in a qualified account, the interest credited to the CD is included in taxable income each year.



In this example, $100,000 is invested in a 10-year CD crediting 3% per year. At the end of 10 years the CD is worth $130,477 due to compound interest. This is very similar to a fixed annuity, excepting that in the event of death the CD is included in the estate of the investor and in probate proceedings unless held in a trust. The fixed annuity is paid out directly to the beneficiary named in the contract. Unlike a fixed annuity, taxes are due every year as the bank credits interest rather than when the CD matures or is cashed in.

CLIENT BENEFITS

- Principal and interest are guaranteed by both the bank and the Federal Deposit Insurance Corporation (FDIC) up to $250,000 per depositor, per insured bank.
- Simple, easy to understand structure.
- Can be purchased in many denominations and durations to align with future spending needs.

RESTRICTIONS AND LIMITATIONS

- Ultra-conservative investments have lower returns over time, making it more difficult to accumulate wealth.
- Interest rates are generally lower than those available in fixed annuities.
- CDs carry penalties for early withdrawals. Unlike annuities, CDs do not generally offer free withdrawal provisions.
- A CD cannot be directly converted to lifetime income.
- Interest earned on CDs is taxable when it is credited by the bank, not when the CD matures and can be liquidated.

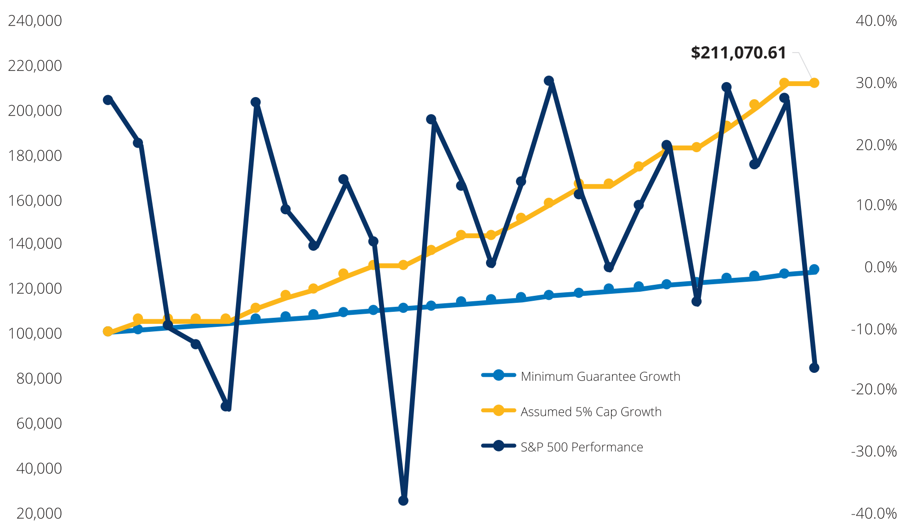
Fixed Indexed Annuities

SUMMARY

Fixed indexed annuities (FIAs) are a type of annuity that offers more upside potential than a traditional fixed annuity with a crediting rate based on the performance of an underlying stock market index such as the S&P 500, Dow Jones, and Nasdaq. FIAs are insurance contracts, not investments or securities, that offer tax-deferred growth with a guaranteed rate of return that provide protection from loss of principal in market downturns, capping both gains and losses. FIAs can be used for guaranteed income through annuitization or the inclusion of a guaranteed income rider.

HOW IT WORKS

An initial contribution is invested by the contract owner and managed in the insurance company's general account. While the contract owner is not invested directly in options, a portion of general account earnings is used to purchase options on market indexes (e.g., the S&P 500). Positive returns on the options result in additional interest credited to the contract. Interest may be credited based on a participation rate, spread, or trigger basis.



In this example using actual S&P 500 return data from 1998 to 2022, the FIA is guaranteed a minimum crediting rate of 1% per year. In years where the change in the S&P 500 is positive, the annuity is credited with the gain in the index, up to 5%. When the change in the S&P 500 is negative no additional interest is credited, and no loss of principal occurs. Over time, and in the volatile stock market conditions shown here, the fixed indexed annuity grows from $100,000 to approximately $211,000, or a compound annual return rate of about 3.2%.

CLIENT BENEFITS

- Tax-deferred growth, and during the income phase clients only pay taxes on the interest earned (for non-qualified FIAs).
- Principal protection and a guaranteed minimum rate of return, subject to the claims paying ability of the issuer.
- The ability to earn interest based on the positive performance of a market index.
- Death benefits ensuring beneficiaries receive no less than the account value and optional enhanced death benefits that may pay out a higher value.
- Ability to annuitize the contract or utilize an income benefit rider to create lifetime income in retirement.

RESTRICTIONS AND LIMITATIONS

- Most contracts have a minimum investment amount, commonly $5,000 to $25,000, and a maximum of $1 million without prior approval.
- The minimum guaranteed surrender value is typically 87.5% of premium. The contract must be held to maturity for 100% principal protection.
- Annual withdrawals exceeding the surrender charge free amount may be subject to an early withdrawal penalty (surrender charge) during the first several contract years.
- Most FIAs are "spread products" without explicit fees (other than for optional benefits). Fee-based products are available with fees up to 1.5% of the account value.
- Guaranteed interest is generally lower than that credited by a fixed annuity, but potential returns are higher due to index-based crediting.

Fixed Income + Index Call Options

SUMMARY

For a given investment amount, a CD, Treasury security, or corporate bond is purchased that will grow to equal that amount plus one percent at maturity. The difference between the value of the fixed income security at maturity and its cost is used to purchase options on the S&P 500 (or other) index or indexes.

HOW IT WORKS

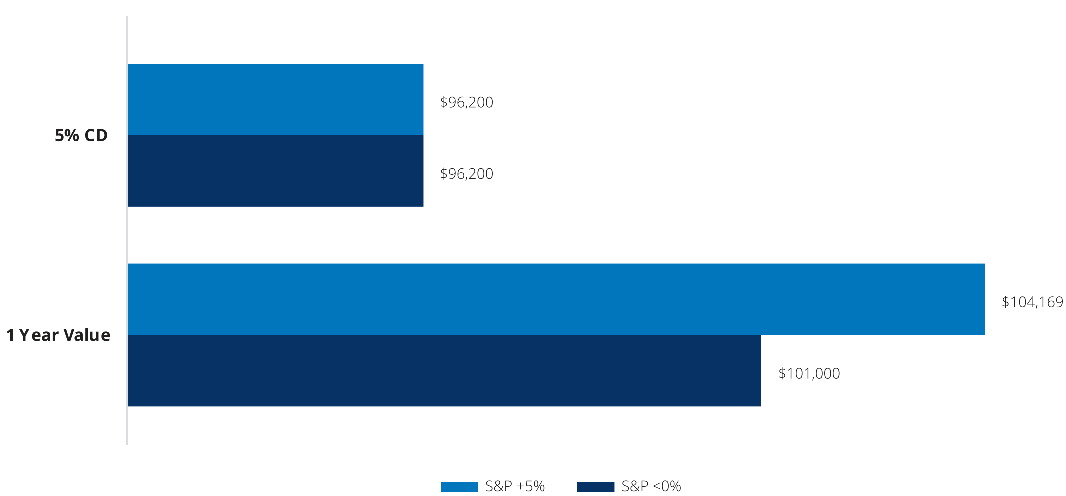
The discounted purchase price of the CD or bond grows to equal the total initial investment, or the total investment plus some interest when the instrument matures. Coincident with the maturity of that security, the options are either sold "in the money," i.e., the S&P 500 index has increased in value and the options are worth more than when purchased, or they expire worthless. This options concept is referred to as "moneyness." The total return is equal to the interest on the fixed income security plus the profit realized from the options trades, if any. This mimics the basic structure of an FIA — a minimum fixed rate of return and a portion of any gain in the index (options profit). The options strategy may be a simple purchase of call options, or the simultaneous purchase of an in-the-money call and sale of an out-of-the-money call, making the options cheaper and providing a higher participation rate in the gain of the index, if any.

CLIENT BENEFITS

- > Provides principal protection if strategy is held until maturity.
- > Many different indexes and options strategies can be utilized.
- > May be easier to exit than a fixed indexed annuity if a significant change in portfolio strategy is desired.

RESTRICTIONS AND LIMITATIONS

- > Requires knowledge of options trading as well as frequent monitoring and trading.
- > Earnings are not tax deferred.
- > Guaranteed lifetime income is not directly available in conjunction with the strategy.



In this example, $100,000 is the total investment. $96,200 is invested in a 5% one-year CD, which will mature at $101,000. The remaining $3,800 is used to purchase one-year SPDR S&P 500 ETF Trust (SPY) calls at a strike price of $398 when the index is at $3,790.30. After one year, if the S&P is up 5%, the total return will consist of $1,000 from the CD and a $3,800 profit from sale of the options, for a total of $104,169 or a roughly 83% participation rate versus the return if the initial investment received 100% of the index return. If the S&P is flat or down, the options expire worthless, and the return is limited to the interest on the CD.

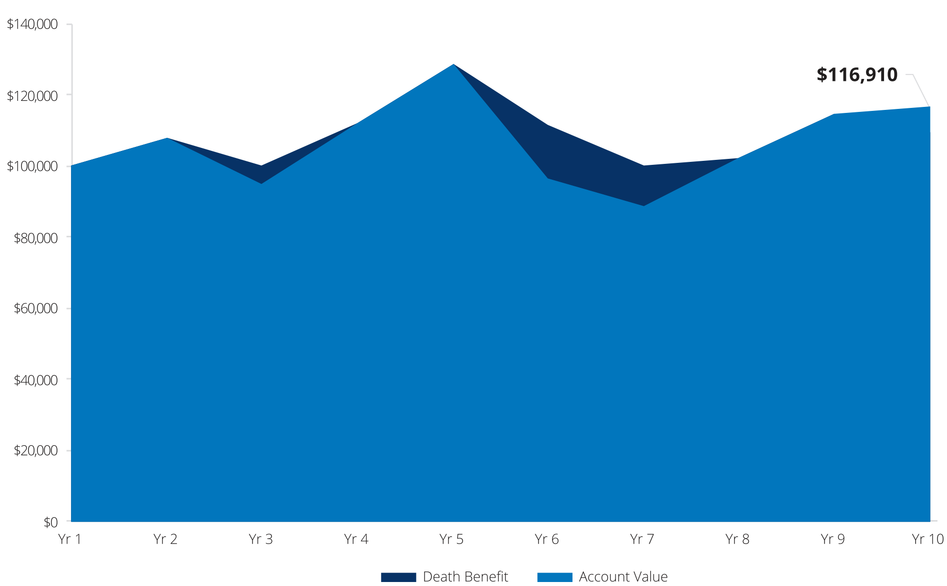
Variable Annuities

SUMMARY

Variable annuities (VAs) are insurance contracts that are considered securities that allow tax-deferred growth by investing the premium in investment subaccounts that resemble open-end mutual funds. These subaccounts invest the premium in pools of different assets like stocks, bonds, money market funds, and in most VAs, a general account option. Variable annuity subaccounts are open-end mutual fund share classes created specifically for use by VAs. Most VAs include optional riders for a fee that offer principal or income protection during the life of the owner and to the beneficiary. These may include enhanced death benefits, guaranteed lifetime withdrawal benefits (GLWBs), guarantee lifetime accumulation benefits (GMABs), and guaranteed lifetime income benefits (GMIBs).

HOW IT WORKS

An initial purchase payment is invested by the contract owner and allocated among the subaccounts and general account of the insurer. Contracts may be funded with a single purchase payment or funded over time subject to minimums and maximums defined by the issuer. Funds in the annuity can be withdrawn, the contract can be "annuitized" (converted to lifetime income payments), or funds may be paid out to beneficiaries upon the death of the contract owner. The death benefit will be no less than the account value, less any surrender charges that may apply. However, most contracts include a standard death benefit that pays the beneficiary no less than the amount invested and waives surrender charges in the event of the owner's death.



In this example, $100,000 is invested in the annuity and the contract owner dies 10 years after the contract is issued. At time of death the accumulated value of $116,910 is higher than the amount invested so the full value is paid to the beneficiary. However, had death occurred at a point when negative returns lowered the accumulated value, the full amount invested would have been paid instead.

CLIENT BENEFITS

- > Investing on a tax-deferred basis without being subject to the limitations currently in place on qualified plans (401(k), IRA, Roth IRA, etc.)
- > Principal protection through return of premium death benefits, if included in the contract, ensuring beneficiaries receive no less than the amount invested.
- > Ability to annuitize the contract to create lifetime income in retirement.
- > Portfolio rebalancing and investment changes can be made without tax consequences.
- > Higher potential returns based on market performance and reinvested dividends.

RESTRICTIONS AND LIMITATIONS

- > Most contracts have a minimum investment amount, commonly $5,000 to $25,000, and a maximum of $1 million without prior approval.
- > Annual withdrawals exceeding 10% of the amount invested may be subject to an early withdrawal penalty (surrender charge) during the first several contract years.
- > Most contracts include annual fees that pay for the distribution and administration of the annuity and the basic return of premium death benefit in the contract.
- > Risk of loss of principal due to market losses, benchmark risk and return dilution.

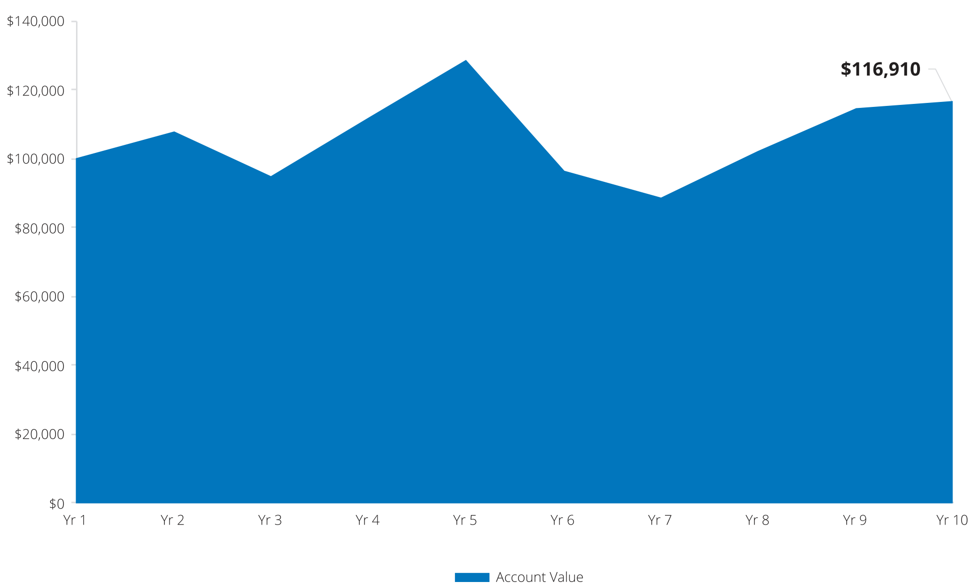
Open-end Mutual Funds

SUMMARY

Open-end mutual funds are SEC registered pooled investment portfolios that buy and sell securities on behalf of investors in the fund. Mutual funds are priced daily, highly liquid, and diversified. A wide range of investment strategies are available to enable advisors to build portfolios aligning with a client's financial goals and risk tolerance.

HOW IT WORKS

An investment account is opened with an online broker or through a financial professional (also called a financial advisor or investment advisor). A strategy is decided upon and mutual funds aligning with the strategy are purchased, either on an ad hoc basis or by setting up a regular investment plan.



In this example, $100,000 is invested in the mutual fund. Its value rises and falls as the stocks and bonds held in the mutual fund portfolio fluctuate in price and dividend and capital gains are reinvested. In the example the ending value of $116,910 is the same as in the VA example, but mutual funds have no insurance features, and therefore the cash value of the fund is always equal to the value of the underlying securities.

CLIENT BENEFITS

- Professional portfolio management.
- Convenience.
- Fair pricing.
- Diversification — losses due to poor performance of a single security are mitigated.
- Higher potential returns based on market performance and reinvested dividends.

RESTRICTIONS AND LIMITATIONS

- No guarantees.
- Tax inefficient; unless held in a qualified account (e.g., 401(k) or IRA), interest and capital gains are taxable when distributed or reinvested by the fund. Shares must be redeemed or other sources of capital must be used to satisfy tax liabilities, and it is possible to have net investment losses and tax liabilities in the same year.
- Benchmark risk (fund returns may deviate from benchmarks).
- Return dilution — the flip side of diversification, return dilution limits participation in returns from high performing securities.

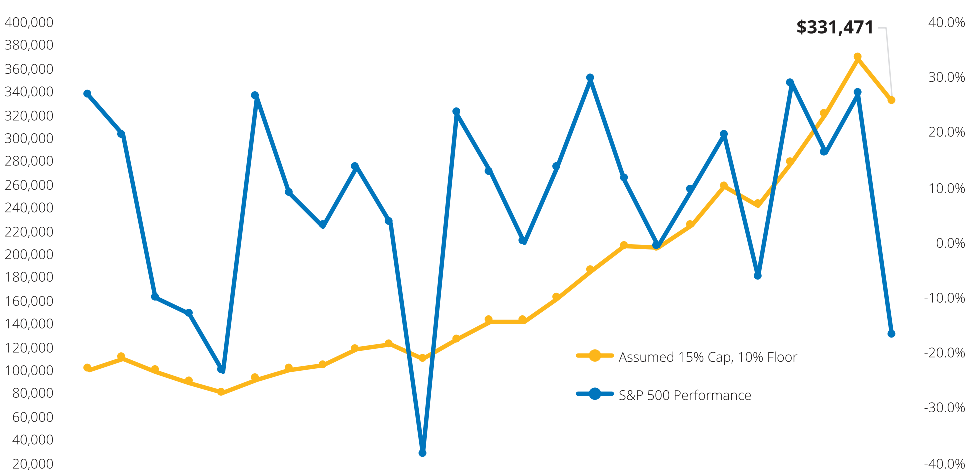
Registered Index-linked Annuities I — Floor Strategy

SUMMARY

Registered index-linked annuities (RILAs) utilize options strategies to provide both upside potential and downside protection. The contract owner is not directly invested in the securities that underlie the index, but rather receives a return on investment based on the performance of the options.

HOW IT WORKS

The initial contribution is held in a segregated separate account managed by the insurance company. Earnings from this account are used to purchase options on one or more market indexes, the most common being the S&P 500 index. In a floor strategy, the client is protected from losses beyond a set percentage, with gains capped at a predefined percentage. As an example, a 10% floor and a 15% cap limits loss to 10% if the index drops 25% and caps the gain at 15% even if the index rises 25%.



In this example using actual S&P 500 return data from 1998 to 2022, $100,000 is invested in the annuity. In years when the S&P 500 has a positive change in value, the RILA account value increases up to 15%. In years when the change in the value of the S&P 500 is negative, losses are limited to 10%. The insurance company absorbs losses beyond the 10% floor. The RILA outperforms the S&P 500 due to market volatility and the years the S&P 500 experienced significant losses, and the annuity grows from $100,000 to $311,741, or a compound annual return rate of about 5.1%.

CLIENT BENEFITS

- Upside potential is greater than in conservative fixed income investments.
- The client receives a measure of principal protection by giving up some upside potential.
- Losses are limited to the preset floor percentage.
- The client is more likely to stay invested and accumulate greater savings for retirement than with a very conservative investment strategy.
- Attractive investment options in a volatile equity market where consumers want greater upside potential than a FIA, fixed annuity, or CD can offer.

RESTRICTIONS AND LIMITATIONS

- Principal protection is generally less than 100 percent in RILA products.
- Gains are limited to the preset cap percentage.
- Only certain indexes are available.
- Index gains do not include dividend income.

Managed Floor ETFs

SUMMARY

Managed floor ETFs use a laddered options strategy to target a maximum level of loss while seeking to achieve incremental positive returns. The options strategies used in the ETF are designed to provide upside potential with call options while targeting a loss "floor," for example limiting losses to 10 percent, using put options.

HOW IT WORKS

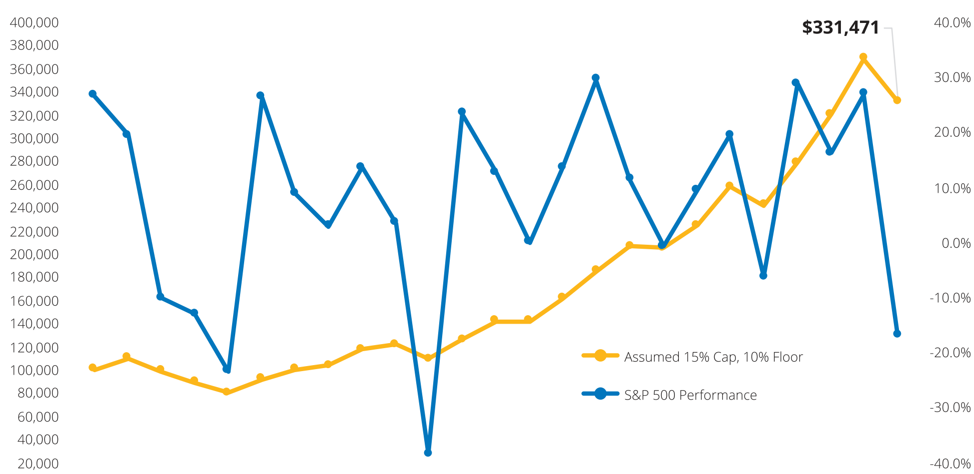
Exchange-traded put option contracts are purchased to provide a floor against significant losses in the target market indexes. Short-dated call options are simultaneously sold with the objective of generating incremental returns above and beyond the cost of the put options. Capital appreciation of the underlying holdings and the incremental returns from the call options are intended to generate positive returns for investors over the long term, while limiting losses.

CLIENT BENEFITS

- Upside potential, which can be described as "equity like," is greater than in conservative fixed income investments.
- The client receives a measure of principal protection by giving up some upside potential.
- Intended to limit losses to a defined percentage.
- The client is more likely to stay invested and accumulate greater savings for retirement than with a very conservative investment strategy.
- May include dividend returns depending on the specific product chosen.

RESTRICTIONS AND LIMITATIONS

- Requires frequent maintenance and trading.
- Loss limits and return goals are targets, not guarantees.
- Insured principal protection and lifetime income are not directly available.
- Gains are not tax deferred.
- May not include dividend returns depending on specific product chosen.



From an illustration perspective, a managed floor ETF is similar to a RILA using a floor strategy; that is, the downside is limited to a 10% loss while the upside is capped. In the case of the ETF, the upside cap is not defined but rather a result of the gains and losses stemming from the options trades. For simplicity, the same 15% upside cap shown for the RILA floor strategy is used here, with the same result in terms of the ending account value. Note, however, that the difference in tax treatment of the annuity and the ETF would have a material impact on the net result..

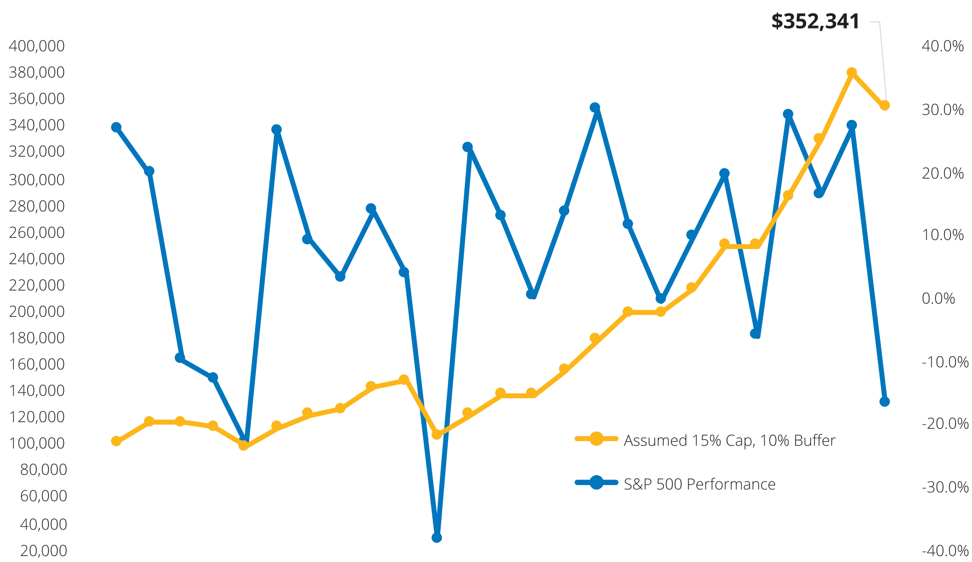
Registered Index-linked Annuities II — Buffer Strategy

SUMMARY

RILAs utilize options strategies to provide both upside potential and downside protection. The contract owner is not directly invested in the securities that underlie the index but rather receives a return on investment based on the performance of the options.

HOW IT WORKS

The initial contribution is held in a segregated separate account managed by the insurance company. Earnings from this account are used to purchase options on one or more market indexes, the most common being the S&P 500 index. In a buffer strategy, the client is protected from losses up to a set percentage, with gains capped at a predefined percentage. As an example, a 10% buffer with a 15% cap will protect against losses up to 10% , resulting in a 15% loss if the index drops 25%, while the cap limits annual gains to 15%.



In this example using actual S&P 500 return data from 1998 to 2022, $100,000 is invested in the annuity. In years when the S&P 500 has a positive change in value, the RILA account value increases by the lesser of 15% or the actual change in value of the index. In years when the change in the value of the S&P 500 is negative, losses are protected up to 10%. The client absorbs losses beyond the 10% buffer. There is no guaranteed minimum return, and in this example the RILA grows to $352,341 and the account experiences far less volatility and reduced losses when the S&P drops significantly.

CLIENT BENEFITS

> Upside potential is greater than in conservative fixed income investments.

> The client receives a measure of principal protection by giving up some upside potential.

> Client is protected against losses up to a set percentage.

> The client is more likely to stay invested and accumulate greater savings for retirement than with a very conservative investment strategy.

> Income benefit riders may be available.

RESTRICTIONS AND LIMITATIONS

> Principal protection is generally less than 100 percent in RILA products.

> Losses beyond the buffer are unlimited.

> Only certain indexes are available.

> Index gains do not include dividend income.

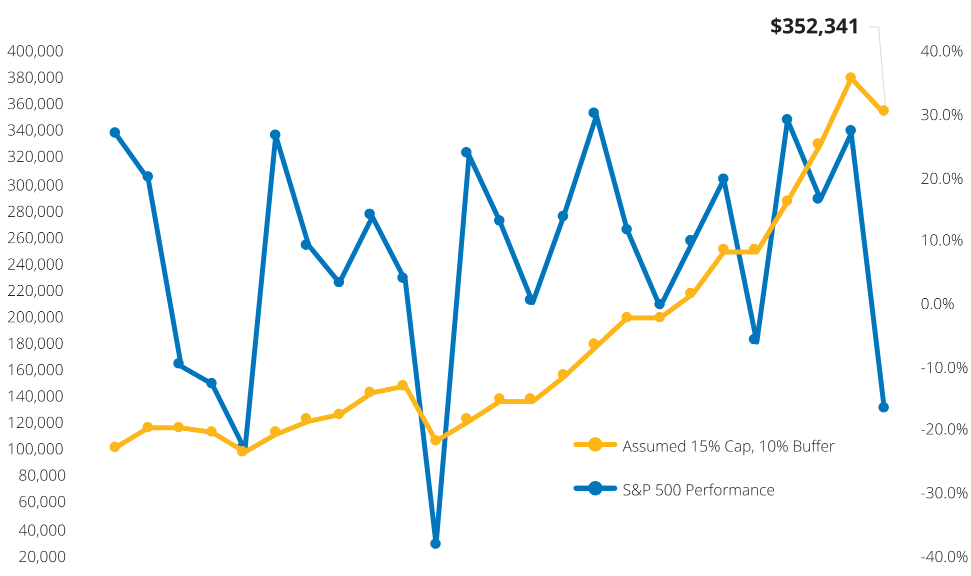
Buffered ETFs

SUMMARY

Buffered ETFs use a laddered options strategy to target a maximum level of loss while seeking to achieve incremental positive returns. A buffered ETF is designed to provide investors with the upside of an asset's returns, up to a capped percentage, while also providing downside protection on a percentage of losses, for example on the first 10 or 15 percent. Buffered ETFs typically have one-year outcome periods.

HOW IT WORKS

A typical buffered ETF purchases one-year call options on a market index, allowing it to purchase the index at the current price in one year. It will also buy put options to provide protection and sell calls to generate premium income that is intended to defray the cost of the put options and generate additional incremental returns.



From an illustration perspective, a buffered ETF is like a RILA using a buffered strategy; as in the RILA, in this example the downside is protected up to a 10% loss while the upside is capped. Unlike the RILA, in the case of the ETF the upside cap is not defined but rather is the result of the gains and losses stemming from the options trades. For simplicity a 15% cap is used in the chart. The ending value is the same as in the buffered RILA example, but again taxes would impact this result.

CLIENT BENEFITS

- Upside potential is greater than in conservative fixed income investments.
- The client receives a measure of principal protection by giving up some upside potential.
- Losses are only incurred beyond a set percentage.
- The client is more likely to stay invested and accumulate greater savings for retirement than with a very conservative investment strategy.

RESTRICTIONS AND LIMITATIONS

- Gains are less than the return of the underlying index.
- Loss limits and return goals are targets, not guarantees.
- Insured principal protection and lifetime income are not available.
- Gains are not tax deferred.
- Do not typically include dividend return.
- Requires frequent maintenance and trading.

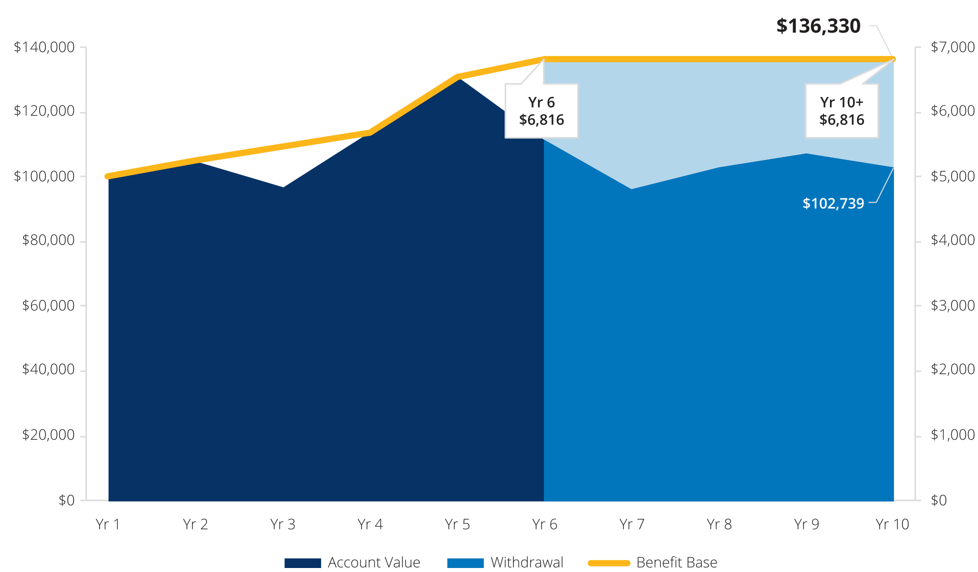
Living Benefits I — Guaranteed Lifetime Withdrawal Benefits

SUMMARY

Living benefits, as the name suggests, provide benefits to annuity owners while they are still alive, most notable a minimum amount of income from an annuity for as long as they might live, even if the annuity value goes to zero. The most common is the GLWB, which provides income through regular lifetime withdrawals of a set amount. GLWBs are optionally available for an additional fee on many VAs and FIAs as well as some RILAs and fixed annuities.

HOW IT WORKS

An initial purchase payment is invested by the contract owner. A "benefit base" is initially equal to the amount invested and may increase at a fixed rate prior to income payments beginning and on contract anniversaries before and after income payments begin if positive investment returns cause the account value to exceed the current benefit base. Income is taken through lifetime guaranteed withdrawals calculated against the benefit base.



In this example, $100,000 is invested in the annuity and withdrawals begin after five years. Prior to the start of withdrawals, the benefit base increases each year due to either positive investment performance (step-up) or annual increases based on a fixed percentage rate. Once withdrawals begin, the guaranteed withdrawal amount may still increase if returns increase the contract value more than withdrawals, negative returns and fees reduce it. If the account value is depleted to $0, income is paid out of the insurance company's general account.

CLIENT BENEFITS

- The client receives regular payments guaranteed for life, or two lives in the case of joint life benefits, to supplement Social Security retirement benefits and other sources of retirement income, such as pensions.
- Unpaid account value may be distributed to beneficiaries upon the death of the owner(s).
- The guarantee itself may give the client more confidence to remain invested during periods of high market volatility, potentially increasing overall portfolio returns in the long run.
- Many GLWBs allow additional penalty-free withdrawals to satisfy required minimum distribution (RMD) rules.

RESTRICTIONS AND LIMITATIONS

- If the contract value becomes zero, payments will continue and will not increase or decrease, will cease at the death of the owner(s), and in some contracts the income amount may be reduced.
- There may be a limited menu of investment options, or some riskier options may not be available, when a GLWB is elected.
- If excess withdrawals are taken the guaranteed amount will be reduced, usually on a pro-rata basis, and in some cases is no longer payable for life.

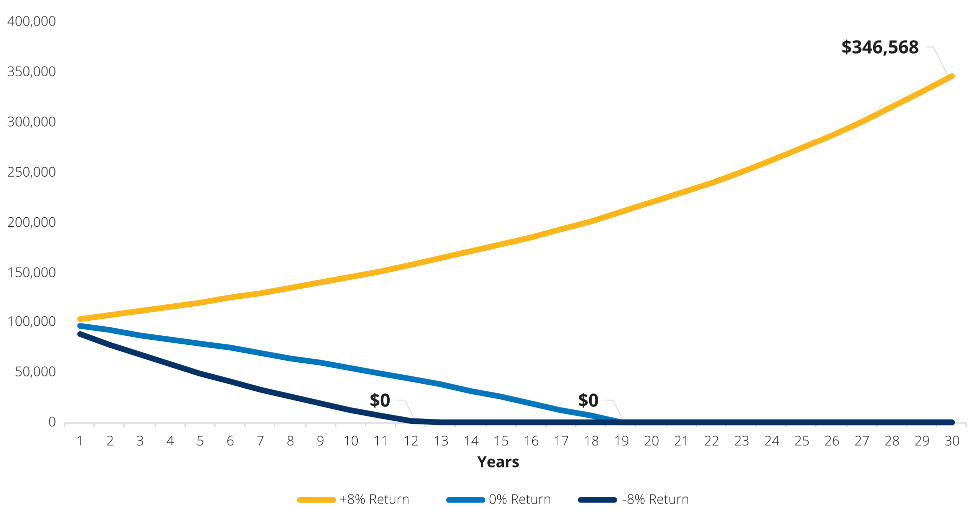
Systematic Withdrawal Plans

SUMMARY

A systematic withdrawal plan (SWiP) is a method of generating regular retirement income from an investment portfolio by systematically withdrawing set amounts, usually on a monthly basis. A SWiP is generally actively managed, using a diversified portfolio of investments. Withdrawals may be taken from a combination of qualified assets (e.g., 401(k) and IRA) and non-qualified assets, requiring careful consideration of the differences in taxation of these assets, as well as special rules for qualified assets such as RMDs.

HOW IT WORKS

The initial withdrawal is calculated as an amount that will provide sufficient supplemental income to the client and also be sustainable over many years during retirement. The so-called "4% rule," where the initial withdrawal is 4% of the total portfolio value, is often used as a starting point. Subsequent withdrawals are typically increased annually to offset increased spending needs due to the impact of inflation.



$100,000 is invested in a mutual fund portfolio and withdrawals begin at $4,000 per year, or 4% of the portfolio value, and are increased each year using a 3% inflation assumption. In the positive case, where returns average 8% annually, the account value continues to grow, reaching $346,568 as earnings exceed withdrawals. If returns average 0% the portfolio is depleted in about 19 years, and at -8% it takes about 12 years for the portfolio value to reach zero. In all three scenarios, the withdrawal amounts are the same but reach over $9,000 annually in the 8% return scenario and end at about $5,500 after 12 years in the -8% example.

CLIENT BENEFITS

> The client receives regular monthly payments to supplement Social Security and any other sources of retirement income, such as a pension.

> The account remains fully liquid, permitting ready access to additional funds if needed; however, additional withdrawals increase the likelihood of funds running out while the client is still alive.

> Tax harvesting can be employed to manage tax liability (selling off investments with capital losses first to provide tax deductions).

RESTRICTIONS AND LIMITATIONS

> No guarantee systematic withdrawals will be sustainable for the life of the client(s); funds may be depleted entirely or systematic withdrawal amounts significantly reduced to preserve principal.

> No principal protection.

> Increases in income due to gains in the portfolio cannot be locked in, as with step-ups in a GLWB.

> No death or lifetime income benefits are available in a mutual fund portfolio.

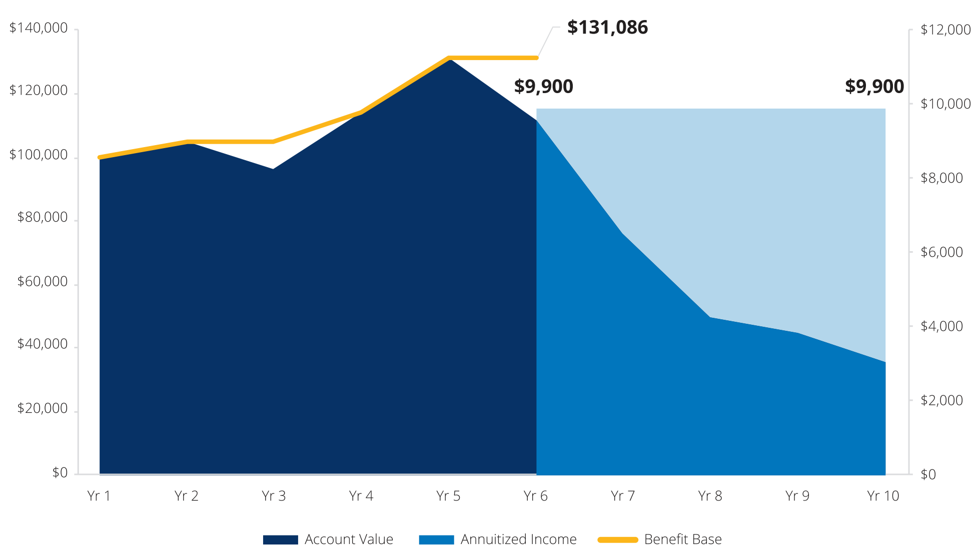
Living Benefits II — Guaranteed Minimum Income Benefits

SUMMARY

GMIBs provide annuitants with a guaranteed lifetime income payment through annuitization of a minimum contract value after a set period, usually 10 years. Annuity payments are calculated against the guaranteed benefit base if that value is higher than the actual account value. GMIBs are available for an additional fee on some VAs.

HOW IT WORKS

An initial purchase payment is invested by the contract owner. A benefit base, initially equal to the amount invested, increases at a set rate for 10 years, and may also be stepped up on contract anniversaries if the current contract value is higher. After 10 years the contract may be annuitized using the greater of the current contract value or the benefit base.



$100,000 is invested in the annuity and the contract value of $131,086 is annuitized after 10 years. Prior to annuitization, the benefit base increases each year due to either positive investment performance (step-up) or annual increases based on a fixed percentage rate. Once annuitization occurs, there is no account value to withdraw from and the annuitant receives guaranteed income payments for as long as they live. Like a SPIA, upon death beneficiaries may receive a lump sum benefit or continued payouts for a period of time, depending on the type of annuitization chosen.

CLIENT BENEFITS

- The client receives regular payments guaranteed for life, or two lives in the case of joint life benefits.
- The guarantee itself may give the client more confidence to remain invested during periods of high market volatility, potentially increasing returns in the long run.
- Guaranteed income payments are generally higher than from a GLWB.

RESTRICTIONS AND LIMITATIONS

- While the insurance company guarantees the income amount, there is no guarantee of the contract value or the amount invested.
- There may be a limited menu of investment options, or some riskier options may not be available, when a GMIB is elected.
- Exercising the benefit requires annuitization of the account value; there is no liquidity other than through annuitization features such as cash or installment refund and period certain payments.
- These benefits are less commonly available than they once were.

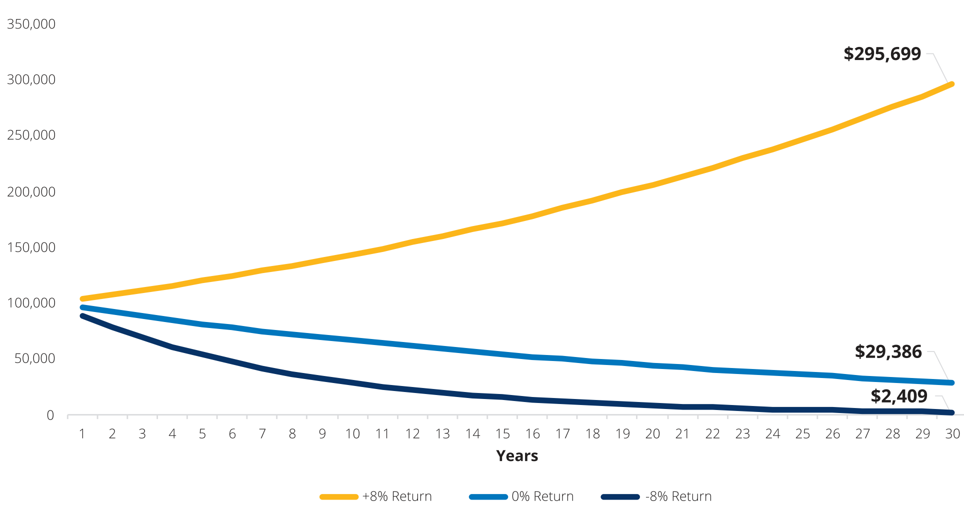
Variable Income Plans

SUMMARY

In a variable income plan, a constant percentage is withdrawn on a regular basis, with the amount of the withdrawal fluctuating based on the returns of a portfolio of investable assets. When the portfolio increases in value, income increases; conversely, when returns are flat or negative and the portfolio decreases in value, income decreases, helping to preserve principal.

HOW IT WORKS

The initial withdrawal is calculated as an amount that will provide sufficient supplemental income to the client and be sustainable over many years during retirement. As opposed to the "4% rule," where income payments start as a set dollar amount and increase by the inflation rate, in a variable income plan the same percentage is taken out each year but the amount fluctuates.



$100,000 is invested in a mutual fund portfolio and withdrawals begin at $4,000 per year, or 4% of the portfolio value. In all cases the portfolio continues for the entire 30-year time horizon. In the positive case, where returns average 8% annually, the account value continues to grow to $295,699 as earnings exceed withdrawals and income payments grow to over $11,000 per year. However, in the negative return scenario performance is poor enough to drive withdrawals down to only $100 per year as the 4% withdrawal rate is applied to a portfolio that has decreased to just a few thousand dollars in value.

CLIENT BENEFITS

> The client receives regular monthly payments to supplement Social Security and any other sources of retirement income, such as a pension.

> The account remains fully liquid, permitting ready access to additional funds if needed; however, additional withdrawals increase the likelihood of funds depleting while the client is still alive.

> Tax harvesting can be employed to manage tax liability (selling off investments with capital losses first to provide tax deductions).

> The portfolio will never be completely depleted.

RESTRICTIONS AND LIMITATIONS

> There are no guarantees systematic withdrawals will be sustainable for the life of the client(s); funds may be depleted to a point where withdrawal amounts must be significantly reduced to preserve principal.

> Funds may be depleted to a point where they fall below minimum account requirements.

> Increases in portfolio value cannot be locked in, as with step-up in a GLWB.

> Poor performance and a long period of withdrawals may reduce income payments considerably.

> No enhanced death or lifetime income benefits are available in a mutual fund portfolio.

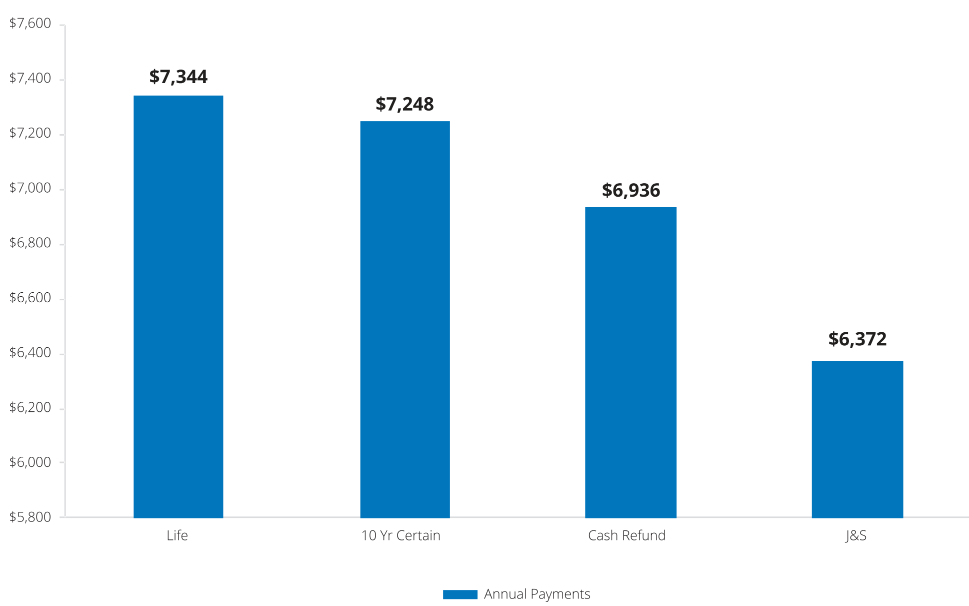
Single Premium Immediate Annuities

SUMMARY

Single premium immediate annuities (SPIAs) provide lifetime income payments in exchange for a lump sum investment.

HOW IT WORKS

An initial purchase payment is invested by the contract owner and deposited to the general account of the insurer. The annuitant (usually the contract owner) receives monthly payments for life, and beneficiaries may or may not receive payments upon the annuitant's death depending on the structure of the annuity.



In this example, $100,000 is invested in the SPIA and payments begin immediately, usually the following month. There is no account value shown on the graph, as the annuitant is only entitled to the payments. The different amounts reflect varying levels of liquidity, i.e., period certain, refund features and joint & survivor (J&S) represent higher guaranteed payments and therefore lower payment amounts.

CLIENT BENEFITS

- The client receives regular payments guaranteed for life, or two lives in the case of joint life benefits.
- Payments may continue after the annuitant's death with period certain, cash refund, and installment refund features.
- SPIAs generally produce the highest amount of guaranteed lifetime income per invested dollar.
- Variable SPIAs invest purchase payments in variable subaccounts. Payments are initially set using an assumed interest rate, and future payments increase or decrease based on actual returns. Few variable SPIAs are available in the market today.
- Some SPIAs may offer a "commutation" feature.

RESTRICTIONS AND LIMITATIONS

- The tradeoff for higher payments is the loss of liquidity; invested funds are only available as annuity payments or beneficiary payments under period certain or refund features, if elected.
- Depending on the terms of the contract and how long the annuitant lives, there may be no death benefit paid to beneficiaries.
- In standard fixed SPIAs, payments do not increase if interest rates rise.

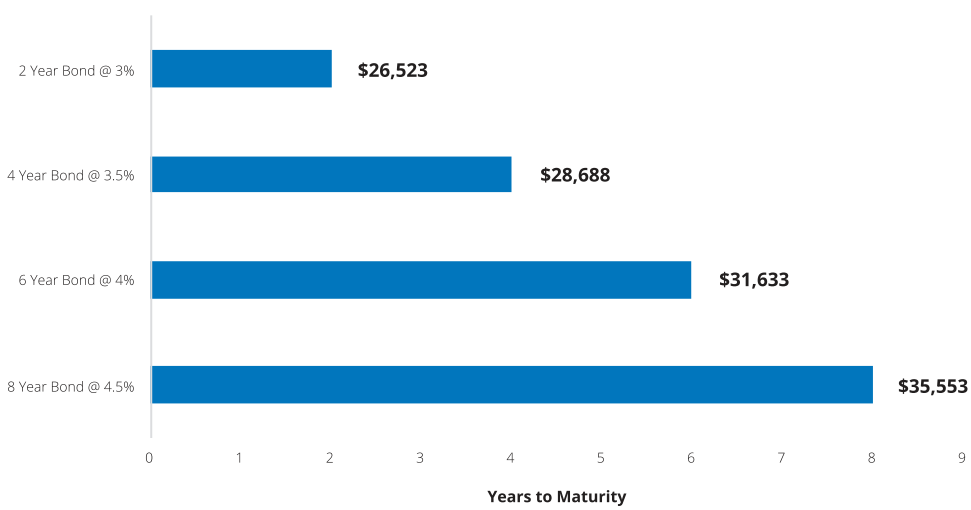
Bond/CD Ladders

SUMMARY

Bonds or CDs of varying duration are purchased. As each bond or CD matures, the proceeds are used to provide retirement income and purchase additional bonds or CDs at the longest duration, extending the ladder.

HOW IT WORKS

The initial purchase is of a series of bonds or CDs of varying duration, for example two, four, six, and eight years. As each bond matures, it is used to purchase another eight-year bond. After eight years, an eight-year bond will be maturing every two years, providing both reinvestment proceeds and retirement income. This helps investors take advantage of the higher rates associated with longer maturities while eventually providing a steady stream of maturing bonds that can be rolled into those longer maturities when older bonds mature.



A bond ladder is simply a series of fixed income purchases designed to ensure a bond is regularly maturing to both provide retirement income and take advantage of fluctuating interest rates. Here, equal investments of $25,000 are made in four bonds or CDs of varying duration. Every two years, the proceeds from the maturing bond (less monies used for supplemental retirement income) are used to purchase another eight-year bond, extending the ladder an additional two years.

CLIENT BENEFITS

- Simplicity and liquidity.
- The client receives regular payments from the bonds or CDs.
- Principal can remain intact if bond interest is sufficient to provide supplemental retirement income.

RESTRICTIONS AND LIMITATIONS

- Income will generally be lower than that provided by SPIAs because there is no mortality pooling component to the payments.
- Low interest rates may result in very little income if principal is not tapped.
- Rapidly rising rates can significantly reduce bond values, especially those of longer duration.
- As bonds mature, the new purchase is subject to the current rate environment which could negatively impact ongoing interest payments if rates have fallen significantly.

Definitions of Key Terms

Accumulation phase: The period of time prior to annuitization or surrender when amounts invested in an annuity accrue interest, dividends, and/or capital gains.

Annuity: An insurance contract that provides future income in exchange for present contributions. It is a long-term investment designed to help protect investable assets and mitigate the risk of outliving income.

Annuitant: The individual entitled to payments made by the annuity and whose age and gender is used to determine the payment amount. The annuitant is usually also the contract owner but may be another person, such as a spouse.

Annuitization: Annuitization is the conversion of the contract value of a deferred annuity into a lifetime stream of income payments, or payments for a set period, or the greater of the two. There are several options to choose from when annuitizing; options that provide a greater guarantee of continuing payments generally result in lower initial payments:

> **Life only:** Payments begin immediately and continue for the life of the annuitant. Payments cease at death, and there is no death benefit paid, even if only one payment was made.

> **Life with period certain:** Payments continue for the longer of the annuitant's life or a set number of years; five, 10, 15, and 20 year certain periods are commonly available.

> **Life with cash refund:** If the annuitant dies before the total of payments made is equal to the amount annuitized, the difference is paid out in a lump sum to beneficiaries.

> **Life with installment refund:** If the annuitant dies before the total of payments made is equal to the amount annuitized, the difference is paid out in installments to beneficiaries.

> **Joint & survivor:** Payments continue until the second of two annuitants dies. Payments may continue at the same amount or at some percentage of the original payment, generally 75%, 66²/₃%, or 50%. When payments reduce after the first death, the initial payment will be greater.

Benchmark risk: The potential for the investment returns of a mutual fund or subaccount to differ significantly from its benchmark (the market index it is measured against).

Benefit base: A value used to calculate a benefit in an annuity, most commonly a lifetime withdrawal benefit. The benefit base value is "notional," i.e., it does not represent contract or cash value but is only used to calculate the value of a benefit.

Beneficiary: The person, persons, or entity legally entitled to receive benefits from financial products. For annuities, these are contractual benefits paid upon the death of the owner, or owners, of the contract.

Bonds: Debt obligations issued by federal, state, and local government agencies or private companies. For example, treasury securities are debt obligations issued by the United States Department of the Treasury, including bills, notes and bonds of varying maturities that pay interest on a semi-annual basis. Corporate bonds are debt obligations issued by a private company. Investment-grade, or "high-grade" bonds have a lower risk of default and higher ratings from credit rating agencies such as Moody's, S&P and Fitch. High-yield corporate bonds offer higher rates of interest but are considered to be at greater risk of default.

Buffered ETF: Exchanged traded funds that provide investors with the upside of a market index, capped to a certain percentage, while also providing downside protection on the first pre-determined percentage of losses. As opposed to a Managed Floor ETF, the investor absorbs losses beyond this pre-determined percentage.

Cash value: The value of a financial product, less any fees or penalties, when fully liquidated. For annuities, also see surrender value.

Certificate of deposit (CD): A bank issued savings product that earns interest on a lump sum investment for a specified period.

Claims paying ability: The financial strength and relative ability of an insurance company to pay claims on its issued annuity and other insurance contracts. Claims paying ability is evaluated by rating agencies such as AM Best, Moody's, Standard & Poors, and Fitch. Rating agencies are businesses that assess the creditworthiness of issuers of annuities and fixed income securities for investors. The likelihood the debt of issuers, such as corporations and governments, is repaid in whole or part, is expressed in ratings arranged in a credit quality scale.

Commutation: A feature that may be available after a contract has been annuitized where future payments are converted to a lump sum, calculated as the present value of the remaining payments based on the life expectancy of the annuitant.

Contract anniversary: The date the contract is issued.

Contract owner: The individual who owns the annuity contract and has the authority to make withdrawals, change beneficiaries and terminate the annuity.

Contract value: The full value of the annuity, not including any early withdrawal penalties that may apply. This may also be referred to as the "account value."

Contract year: The one-year period between contract anniversaries.

Corporate bond: A debt obligation issued by a private company. Investment-grade, or "high-grade" bonds have a lower risk of default and higher ratings from credit rating agencies such as Moody's, S&P and Fitch. High-yield corporate bonds offer higher rates of interest but are considered at greater risk of default.

Death benefit: The amount an annuity contract pays to the contract owner's named beneficiary or beneficiaries upon the death of an owner or co-owner.

Deferred annuity: A contract with an insurance company that promises to pay the owner a regular income or lump sum at some future date. Interest and capital gains in fixed and variable annuities are not taxed until monies are withdrawn.

Dividend return: The portion of the overall return of a stock attributable to dividends paid per share by the issuing company.

Duration: The length of time it takes for an investor to recover the price paid for a bond from total cash flows (principal plus interest). It is also a measure of the sensitivity of the bond's price to changes in interest rates. The prices of bonds of longer duration (e.g., 30-year Treasuries versus 10-year Treasuries) will experience greater changes when interest rates rise or fall.

Early withdrawal penalty: Also called a "surrender charge," this is a type of sales charge that may be assessed if you withdraw money from an annuity during the surrender period defined in the contract. This charge allows the insurer to cover issuing and maintenance costs for policies surrendered before such costs are recovered. Most surrender charge periods are three to seven years with the charge reducing by one percent per year until it reaches zero.

Enhanced death benefit: Standard annuity death benefits are generally equal to the current account value or the greater of the account value or amount invested (return of premium, or ROP). Enhanced benefits may use roll-ups, step-ups, or both to provide a higher level of protection for beneficiaries.

Exclusion ratio: The percentage of annuity payments that is not subject to taxes and is excluded from gross income. It is calculated by dividing the initial investment over the expected payment period, which for lifetime annuity payments is equal to life expectancy. For example, if a payment of $7,500 per year is made to a 65-year-old male annuitant with a 20 year life expectancy and the amount invested was $100,000, $5,000/$7,500, or 66.67%, or each payment is not subject to income taxes until the amount invested is recovered. After 20 years the $7,500 payment is fully taxable at ordinary income rates.

Federal Deposit Insurance Corporation (FDIC): The Federal Deposit Insurance Corporation (FDIC) is an independent agency created by Congress to maintain stability and public confidence in the nation's financial system. To accomplish this mission, the FDIC insures deposits; examines and supervises financial institutions for safety, soundness, and consumer protection; makes large and complex financial institutions resolvable; and manages receiverships. The standard insurance amount is $250,000 per depositor, per insured bank, for each account ownership category.

Fees: Most fixed annuities do not charge explicit fees, except for optional benefits, but are spread products. Variable annuities typically have a few different fees:

> Mortality & expense risk (MER) fees, which cover costs related to distributing the product.

> Administrative fees, which cover costs associated with managing the product over time.

> Investment management fees, which are paid to the professional investment management firms that create and manage the subaccounts offered in the annuity.

> Fees for optional benefits, which pay for additional death benefits, principal protection, or income guarantees.

FIA spread: The percentage subtracted from the index change before interest is credited to the FIA. For example, if the index increases by five percent and there is a two percent spread, the interest credited to the contract will be three percent. Spreads do not reduce the contract value if the index change is negative.

Financial goals: Financial priorities that impact the objectives investors set for how to save or spend money during important life stages.

Financial professional: A qualified person who can help investors understand their options and make financial decisions to work toward financial goals.

Fixed annuity: A tax-deferred insurance contract that promises to pay the buyer a guaranteed rate of interest on their contributions and provides a lifetime income stream in retirement. Interest is credited by the insurer based on what they think they will earn on their general account investments.

Fixed indexed annuity (FIA): A FIA is tax-deferred insurance contract that provides principal protection in down markets and an opportunity for growth. FIAs credit a guaranteed interest amount, with the opportunity to earn additional interest based on positive changes in the value of one or more market indexes, such as the S&P 500.

Free withdrawals: An annual percentage of the amount invested that can be withdrawn from the annuity without penalty each year. The penalty-free withdrawal amount can vary between insurers, but 10 percent is common.

General account: The account of the insurer (i.e., annuity issuer) where premiums invested in annuities are deposited and from which the insurer funds business operations. The general account aggregates all funds rather than holding dedicated amounts for specific policies. Fixed annuities and fixed indexed annuities are general account products, and most variable annuities offer a fixed account option that invests in the general account. Registered index-linked annuities may also utilize both general and separate accounts to invest premium depending on the structure.

Guarantee minimum accumulation benefit (GMAB): A benefit that guarantees the account value will equal some fixed percentage (typically 100%) of premiums, minus any withdrawals, as long as the contract remains in-force and the account value does not decrease to zero as a result of withdrawals, after a minimum period of time, usually 10 years.

Guaranteed minimum income benefit (GMIB): A benefit offered in variable annuities that guarantees the contract owner can annuitize the contract and receive annuity payments calculated against the greater of the actual account value or guaranteed benefit base. As with an immediate annuity, there is no cash value after annuitization and payments are made for the life or lives of the annuitant(s).

Guaranteed lifetime withdrawal benefit (GLWB): A benefit offered in variable, fixed indexed and RILAs that allows the contract owner to withdraw a set amount each year. Withdrawals continue for the life of the owner, or the owner and a spouse in the case of joint benefits, regardless of whether there is still account value in the product. Amounts are calculated using the benefit base and are withdrawn from the account value if there is still account value in the annuity. If the account value becomes zero due to withdrawals and/or market performance, the contract enters the settlement phase and the insurance company continues to make payments until the owner(s) die.

Immediate annuities: Also referred to as single premium immediate annuities (SPIAs), these are insurance contracts where a lump sum is invested and the insurance company agrees to make periodic income payments for life, a specified period, or the longer of the two. SPIAs have no cash value beyond the insurer's obligation to make the periodic payments under the terms of the contract.

Investable assets: Assets that can be easily liquidated, such as bank accounts, stocks, bonds, mutual funds and annuities.

Joint life benefits: Annuity income benefits that are issued on two people, usually spouses, and continue to pay to the second person after the first dies. Available as an annuitization option and with most guaranteed lifetime withdrawal and guaranteed lifetime income benefits.

Lifetime income: Periodic income payments from an annuity that continue for the life, or lives, of one or more owners. Lifetime income is available through annuitization, or through living benefits such as guaranteed lifetime withdrawal benefits and guaranteed lifetime income benefits.

Liquidity: The relative ease with which an investable asset can be converted into cash without affecting its market price.

Living benefits: Optional benefits offered on some annuities which provide benefits while the contract owner is still alive. Examples include GMAB, GMIB, and GLWB.

Managed floor ETF: Exchanged traded managed outcome funds that use options strategies to provide investors with the upside of equity markets while providing a measure of downside risk. As opposed to a buffered ETF, the investor is protected against losses beyond a pre-determined percentage.

Market index: A hypothetical portfolio of investment holdings that represents a segment of the financial market. The value of the index is calculated using the prices of the underlying holdings.

Market risk: The chance an investor could lose money because of market downturns.

Market volatility: Also referred to as "market ups and downs," the way stocks, bonds and other market investments change in value, sometimes very quickly.

Maturity: The date a financial agreement ends, triggering repayment of principal with interest.

Moneyness: A term describing the relationship of an option's strike (exercise) price with its spot (market) price. "In the money" options have a strike price greater than the spot price, whereas "out of the money" options have strike prices below their spot prices.

Mortality pooling: Also called "mortality credits," in a large group of annuitants the investments of those who die earlier than expected contribute to the overall pool and provide higher payments to survivors. The mortality credit increases significantly with age (when more individuals in the group are likely to die) and hedges longevity risk, creating a return that would be difficult to match using other financial products or approaches.

Open-end mutual fund: A collective investment vehicle that buys and sells stocks, bonds, and options and can issue unlimited new shares, priced daily based on the net asset value of the securities held in the portfolio.

Option: The right to buy or sell a security at an agreed upon price for a defined time period.

Participation rate: The percentage of the increase in the index value that is credited to the annuity at the end of a selected time period.

Principal protection: Embedded or optional features in an annuity that guarantee the contract will return no less than the amount invested. All fixed and fixed indexed annuities contractually provide 100% principal protection, per the terms of the contract (FIAs return a minimum of 87.5% of principal and must be held to maturity for 100%) and subject to the claims paying ability of the issuer. Variable annuities can provide principal protection through GMABs, and RILAs provide partial principal protection using options strategies. Principal protection for beneficiaries in variable annuities can also be achieved through return of premium death benefits. Non-annuity products and solutions can also provide, but not guarantee, a level of principal protection using options strategies.

Probate: The formal legal process that occurs when a decedent leaves assets to distribute, such as bank accounts, real estate, and financial investments. The probate process involves gathering assets, satisfying debts, and distributing remaining amounts to beneficiaries. Amounts invested in annuities are generally paid directly to named beneficiaries as death benefits and are not included in the probate process.

Purchase payment: Also called premium, this is the payment or series of payments that represent the investment in the annuity.

Qualified plan: An individual or employer-sponsored retirement plan that offers individuals the opportunity to save for retirement on a pre-tax basis — contributions and earnings are not taxed until withdrawn. Individual retirement plans such as individual retirement accounts (IRAs) must meet the requirements of the Internal Revenue Code, and employer-sponsored plans such as 401(K) plans must also meet the requirements of the Employee Retirement Income Security Act (ERISA). Investments made with money that has already been taxed are referred as “non-qualified.”

Registered index-linked annuity (RILA): An insurance contract providing a tax-deferred, long-term savings option that limits exposure to downside risk and provides the opportunity for growth.

Required minimum distribution (RMD): The amount you are required to withdraw annually from a qualified retirement account, such as an IRA, starting at age 72.

Return dilution: The limited participation in the returns of outperforming stocks when held in a widely diversified portfolio. In other words, one or two stocks with very high returns may not contribute much to overall returns in a portfolio of 50 different securities.

Return of premium death benefit (ROP): Pays beneficiaries the greater of the contract value or the total amount invested upon the death of the contract owner(s).

Roll-up: An annuity feature that increases the value of a benefit each year, independently of the contract value, on either a simple or compound basis. For example, a 4% guaranteed lifetime withdrawal benefit with a roll-up feature might increase the benefit base by 5% per year, compounded annually. The annual withdrawal amount would then be the greater of 4% of the account value OR 4% of the compounded benefit base when withdrawals begin. Similarly, a death benefit with a roll-up feature would pay beneficiaries the greater of the current account value or the roll-up value upon the death of the contract owner. Amounts calculated using roll-up percentages do not represent contract or cash value. They are only used to calculate benefit amounts, and those amounts are only accessible through the terms of the benefits in which they are used. Roll-ups generally terminate when benefit payments begin.

Separate account: A fund created by the insurer, separate from the company’s general account, that is used for investing variable annuity and other holdings (such as pensions) in open-end funds and other investments.

Spread: The difference between the interest the insurance company earns on its investments and the interest credited to the annuity. Fixed and fixed indexed annuities are often referred to as “spread products.” The difference covers the insurance companies operating costs and profit.

Step-up: An annuity feature that increases the benefit base to equal the current account value. Step-ups generally occur on contract anniversaries and may be based on the anniversary value or the highest value the contract attained at certain points during the prior year, e.g., the highest value on any day the stock market was in session during the prior year. Step-ups may continue after benefit payments begin, provided there is contract value that has not been paid out.

Subaccount: A segregated account maintained by an insurance company to hold mutual fund-like investments for use in variable annuity and variable life products. Assets held in segregated accounts are not subject to the claims of the insurance company's creditors in the event of bankruptcy.

Surrender value: The cash value of the annuity less any early withdrawal penalty, market value adjustment, charges or fees.

State guaranty associations: State guaranty associations provide coverage (up to the limits spelled out by state law) for resident policyholders of insurers licensed to do business in their state.

Systematic withdrawal plan (SWiP): The withdrawal of fixed amounts from a portfolio of investable assets on a regular, periodic basis (monthly, quarterly, annually) for supplemental retirement income. The dollar amount of withdrawals typically begins as a defined percentage of the portfolio value (e.g., 4%) and is adjusted annually for inflation.

Treasury security: A debt obligation issued by the United States Department of the Treasury, including bills, notes and bonds of varying maturities that pay interest on a semi-annual basis.

Trigger: A method of crediting interest to an FIA where the contract is credited with a stated rate of interest if the change in value of the underlying index is positive over the specified time period.

Trust: A legal entity that holds asset for beneficiaries. The terms of the trust dictate the method and timing of the distribution of assets.

Variable annuity (VA): An annuity with an account value tied to the performance of an investment portfolio. The value of the annuity, and payments from the annuity, can increase if the portfolio performs well and decrease if the portfolio loses money.

Variable income plan: The withdrawal of a set percentage amount from a portfolio of investable assets on a regular, periodic basis (monthly, quarterly, annually) for supplemental retirement income. The dollar amount of withdrawals will vary based on investment returns and the reduction in portfolio value from withdrawals, effectively resulting in a "raise" when the portfolio performs well and a "pay cut" when it does not.

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APPENDIX B

2015 Letter
from
93 House Democrats