Trump administration seeks to give boost to 401(k) annuities

A Treasury proposal seeks to amend rules for plan sponsors to help them assess the long-term viability of insurance companies

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By Greg Iacurci

The Trump administration wants to give a shot in the arm to annuities in 401(k) plans by encouraging rules to make it more palatable for plan sponsors to offer such products.

The Treasury Department issued a report calling for the Labor Department and Treasury to craft proposals on how plan sponsors can get help in assessing the long-term financial strength of annuity providers.

Many employers view current rules around the selection of an insurer as too risky to use, and don't offer annuity products as a result. The Treasury's recommendation is meant to "encourage the availability of in-plan annuity options and promote broader consumer choice," according to the report.

The proposal continues a trend witnessed during the prior administration of promoting the spread of lifetime income in 401(k) plans.

"It started under the Obama administration, and still seems to have legs under the Trump administration," said Andrew Oringer, co-chair of the employee benefits and executive compensation group at Dechert. "They're continuing this percolation of ideas that would push people toward annuities."

Only 5% of 401(k) plans offer products with a retirement income guarantee, according to the Plan Sponsor Council of America. About 12% of plan sponsors are considering adding such a product, though.

Proponents of adding lifetime-income options see it as a way to re-frame retirement savings around drawing down rather than accumulating assets. While pension plans offer a monthly income stream to retirees, DC plans often don't have a mechanism for this sort of annuitization or to help them draw down their assets.

"It's a lump sum of money waiting to be spent rather than a flow of income," Mr. Oringer said

However, not everyone believes broader availability of annuities to plan participants would be a good thing.

Andrew Stoltmann, president of the Public Investors Arbitration Bar Association, believes individuals "should almost never put a tax-deferred savings investment like an annuity into a tax-deferred savings program."

Besides, "these are illiquid, high-cost, high-fee investments that most clients don't understand and don't need," Mr. Stoltmann said. "The only ones out there who want annuities in 401(k)s are those who stand to profit."

The Obama administration issued rules encouraging the use of certain longevity annuities (qualified longevity annuity contracts) in retirement plans, and also gave plan sponsors its blessing to use target-date funds that bundle in deferred annuities.

It also pursued rulemaking that would require participant statements to include income illustrations based on their current account balance. That project wasn't completed by the end of the administration's tenure.

Now, the Trump administration is stepping into the fray.

Under current "safe harbor" rules, meant to protect employers from fiduciary liability, plan sponsors must assess an insurer's ability to "make all future payments under the annuity contract." However, employers view judging an insurer's solvency decades in the future as too risky, observers said. Indeed, plan sponsors cite fiduciary exposure as their top barrier to implementation, with nearly 40% calling it a concern, according to the PSCA.

The Treasury, in its report published Oct. 27, says independent fiduciary assessments could be "in the form of ratings or other specific metrics" to help plan sponsors comply with their fiduciary duty.

The Government Accountability Office last year urged the DOL to update 401(k) annuity rules, but DOL officials believed at the time that doing so would potentially weaken consumer protection.

Aron Szapiro, director of policy research at Morningstar Inc., suspects a legislative fix during this congressional term is more likely than the Treasury and DOL working to issue new rules, given the DOL's workload at the moment, which includes reviewing the fiduciary rule.

The Retirement Enhancement and Savings Act, which would make it easier to offer 401(k) annuities, passed the Senate Finance Committee last year but has yet to make headway in the current Congress.

Plus, observers believe fixing the safe-harbor rules, while useful, wouldn't cause plan sponsors to jump headlong into lifetime income.

Philip Chao, principal and chief investment officer at Chao & Co., points to annuity portability as an additional challenge. If a participant buys into an annuity but changes jobs and wants to transfer the money to a new plan, would they be able to do so, for example?

"Some kind of exchange has to be set up. It gets really complicated, and that's a problem," Mr. Chao said. "Safe-harbor doesn't talk about the plumbing. It only talks about selecting an annuity from a fiduciary standpoint."

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