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Department of Labor Issues Proposed Rules on Selection of Annuity Providers for Individual Account Plans

According to the Department of Labor, a reason often cited by plan sponsors for not offering an annuity option under a defined contribution plan is the fiduciary liability attendant to selecting the "safest available" annuity, the standard required by Interpretative Bulletin 95-1 for both defined benefit and defined contribution plans.

The Pension Protection Act of 2006 ("PPA") directed the DOL to issue final regulations clarifying that the selection of an annuity contract as an optional form of distribution for an individual account plan is not subject to the safest available annuity standard under Interpretative Bulletin 95-1 but is subject to all otherwise applicable fiduciary standards.

The DOL recently issued proposed regulations implementing the PPA mandate which contain a safe harbor for selecting annuity providers and contracts for individual account plans (defined contribution plans):

- The fiduciary must engage in an objective, thorough and analytical search for the purpose of identifying and selecting providers from which to purchase annuities. The process must avoid self-dealing, conflicts of interest or other improper influence and should, to the extent feasible, involve consideration of competing annuity products.

- The fiduciary responsible for the selection of the annuity provider must determine whether he/she has the expertise or knowledge to meaningfully evaluate the annuity provider consistent with the requirements of the regulation.

- The fiduciary must appropriately consider information sufficient to ensure the ability of the annuity provider to make all future payments under the annuity contract.

- The fiduciary must consider the cost of the annuity contract in relationship to the benefits and administrative services to be provided under such contract.

- The fiduciary must conclude, at the time of the selection, that the annuity provider is financially able to make all future payments under the contract, and the cost of the contract is reasonable in relationship to the benefits and services to be provided under the contract.

- If the annuity provider must provide multiple contracts over time, the fiduciary must periodically review the conclusion described in the previous bullet point, taking into account the third and fourth bullet points.

In its consideration of the annuity provider's ability to make all future payments and the cost of the contract in relationship to the benefits and services to be provided, the fiduciary should consider the following:

- The ability of the annuity provider to administer the payment of benefits under the annuity and to perform any other services.
- The cost of the contract in relation to the benefits and services to be provided, taking into account the amount and nature of any fees and commissions.
- The annuity provider's experience and financial expertise in providing annuities of the type being offered or selected.
- The annuity provider's level of capital, surplus and reserves available to make payment.
- The annuity provider's ratings by insurance rating services.
- The structure of the annuity contract and benefit guarantees provided.
- The use of separate accounts to underwrite the provider's benefit obligations.
- The availability and extent of additional protection through state guaranty associations.

The DOL does not believe that this regulation will affect the percentage of participants in individual account plans who will elect annuity options.

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