

The Promise of a Better Retirement: Implementing the Pension Protection Act

ICI President's Remarks at the Pension Protection Act Developments Conference

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Keynote Address by Paul Schott Stevens President, Investment Company Institute

February 7, 2007
Washington, DC

Good morning, and welcome to the Investment Company Institute's conference on the Pension Protection Act of 2006. I'm Paul Stevens, President of ICI, and I'm pleased to open this timely and important meeting.

ICI has convened this conference because we believe the [Pension Protection Act](#) marks a watershed event in our nation's approach to retirement security. All concerned – including regulators, service providers, and plan sponsors – need to work together to ensure that the Act meets its full potential. For the defined contribution retirement system, the 2006 legislation is the most important extension of ERISA since the original act passed more than three decades ago. The new law represents, I think, Congress's recognition that defined contribution plans are now the centerpiece of our private-sector retirement system, and are likely to remain in that central role.

I want to talk briefly about how we got here – and then at more length about where we go from here. We can justly celebrate the successes of defined contribution and the [401\(k\) system](#), which now holds \$2.4 trillion in assets on behalf of 47 million active participants and millions of former employees and retirees. But we must also recognize that there is still a considerable way to go to help all Americans realize their dreams of retirement security.

Our goal should be to make sure that the defined contribution system reaches its full potential in meeting the needs of American workers. That means every worker in America with access to a DC plan taking the fullest possible advantage of the opportunity to save for retirement, with smart investments, from the first day he or she is eligible. It also means expanding the number of workers to whom such plans are available.

How can we achieve this ambitious goal? To answer that question, I think it's instructive to ask another: How has the 401(k) system come so far in its first quarter-century?

Like most successful government programs in our country, the 401(k) reflects a blend of sound public policy and private-sector innovation.

Congress planted the seeds in 1974 with ERISA, and then in 1978 with Section 401(k) of Internal Revenue Code. The new 401(k) system grew despite tight funding limits and regulatory restrictions. Starting in the mid-1990s, the departments of Labor and Treasury began to promote the 401(k) as a potent tool for retirement saving. Public policy in this area has been guided by the sound principles embodied in ERISA: the maintenance of high standards of fiduciary conduct and a central role for clear and useful disclosure, to the benefit of sponsors and participants alike. The Labor Department's Employee Benefits Security Administration has made many

important contributions, particularly in helping to develop rules for self-directed accounts and in educating 401(k) plan sponsors on their fiduciary duties. We are pleased that several of EBSA's officials are on our program and in the audience today.

The 401(k) owes much to the private sector as well – including the mutual fund industry. On the spare legal foundation that Congress provided, we helped build a structure of investment options, recordkeeping, participant education, regular quarterly benefits reports for workers, and information systems to help plan sponsors cope with a thicket of legal requirements. As a result, any company today can go to the market and find a turnkey 401(k) plan – or assemble a customized plan suited to its needs.

That history of innovation is continuing. Promising ideas like automatic enrollment, investment advice for participants, and target-date investments arose from the ingenuity of American employers, benefits experts, and – yes – mutual funds and other financial services firms, all striving to make the system more effective for both sponsors and participants.

Now, with the Pension Protection Act, Congress has granted many of these recent developments a secure place in the law. If this legislation is implemented properly, it undoubtedly will usher in yet another round of innovation that will take 401(k) into a new era of expanding coverage and increasing effectiveness in meeting Americans' retirement needs.

Deserving special mention is one group that has driven much of the growth and success of the 401(k): employers. At its core, ours is a voluntary system. Employers choose whether or not to offer retirement benefits based largely on competitive considerations, including their place in the labor market. So, if we want more Americans to enjoy the fruits of 401(k) participation, the system must continue to attract and engage employers.

But employers are more than just gatekeepers to 401(k). Indeed, their involvement is a major strength of the defined contribution system. ERISA calls upon employers to act with diligence in selecting investment options and service providers, keeping costs in line, maintaining communication with their employees, and educating participants to make the best use of their 401(k)s. All this and more is implicit in the role that employers have as fiduciaries for their employees, the plan participants.

Many employers subsidize their plans as well, not just by absorbing costs of setting up and running a plan, but also by making contributions to workers' accounts. Consistently since the mid-1990s, employers have contributed on average 50 cents for every dollar that participants save. The latest data show that America's employers are contributing nearly \$60 billion a year to 401(k) plans.

If we want retirement security for all Americans, we must ensure that the 401(k) system evolves to draw in more employers. That means that 401(k) plans must be as simple as possible and accessible to even the smallest employers, ones engaged in many different kinds of business.

Experience teaches us that if we build a better 401(k) system, more employers will come. After 25 years of development, the 401(k) system now covers about 50 percent of the active private-sector workforce. It has proven to be highly flexible and adaptable, meeting the needs of companies large and small, with younger and older workers, in a wide range of industries. 401(k) plans appeal to companies of all sizes: according to the Labor Department, three-quarters of 401(k) plans have fewer than 50 participants. And while most companies originally used 401(k)s to supplement their traditional pension offerings, by 2003, more than 90 percent of all 401(k) plans were stand-alone – that is, they were the only retirement vehicle that the employer offers. Some 60 percent of those stand-alone plans were created after 1995.

Clearly, we need to ensure that the reforms of the Pension Protection Act continue to encourage employers to offer more and better 401(k) plans to America's workers. I'm not going to get into the details of the regulations under consideration – on that score, you would do better to hear from the ERISA experts on our panels. But, in the spirit of maintaining this momentum, let me offer some suggestions on three important issues.

First, automatic enrollment and default investments. Later today, Jack Brennan, Chairman of the Vanguard Group, will describe the powerful impact auto-enrollment will have on America's savings habits. But those added savings must be invested wisely, and employers should be encouraged to select default options that are suitable for long-term retirement investing. As the Labor Department has proposed, regulations should define several categories of investments that embody a mix of asset classes and provide diversification. The Department's proposed approach embraces many products that are in the market today – but it will also provide flexibility to encourage innovation and accommodate new products that aren't even on the drawing board yet. After all, today's fastest-growing asset-allocation products, target-date funds, were barely a gleam in their inventors' eyes just 13 years ago. And other products surely will be developed to fit within the framework that the Department crafts for qualified default options.

The second area that deserves attention is investment advice. Employers long have wanted to help their employees make smart choices with their 401(k) balances. Regulations have accommodated this desire by permitting companies to offer third-party investment advice. The language of the Pension Protection Act is hardly a model of clarity, but it seems certain that the 109th Congress intended to expand advice offerings, not shrink them. The Labor Department took an important step last week by releasing immediate guidance on several key issues. We are fortunate to have the author of that guidance, Bob Doyle, on our first panel today.

Still, many issues remain open, including the mechanics of how advice is provided and the feasibility of using computer models to give advice to owners of Individual Retirement Accounts. Here, too, the guiding principle must be Congress's intention to give participants easier access to high-quality investment advice, subject to fiduciary and disclosure safeguards.

Thirdly, the PPA charges the Department with designing specifications for the quarterly statements that participants in self-directed 401(k) plans must receive. At ICI, we have done extensive research on the challenges of meeting the information needs of average investors. Everything we have learned confirms that more data typically does not translate into deeper understanding. Consistently, our studies show that investors want and need clear, concise statements that focus on the key factors – performance, risks, and fees – that drive their investment decisions. I would urge the Labor Department to craft standards that will help all plans address the needs of their participants for meaningful information about their accounts. The useful statements that many 401(k) plans already provide participants to help them understand their accounts can serve as a model here.

While our focus today is on the Pension Protection Act, I can hardly discuss disclosure for 401(k) plans without taking note of some larger issues that have been identified in this area. Representative George Miller, the new Chairman of the House Education and Labor Committee, has signaled his strong interest in the operations of the 401(k) system and has announced his intention to hold hearings to review how 401(k) fees are set and are disclosed. We commend Chairman Miller for his focus on improving the 401(k) system, and we look forward to working with him and his Committee.

The mutual fund industry has been urging improvements in the area of 401(k) disclosure for a very long time. In 1976 – at the very dawn of the ERISA era – the Institute advocated [QUOTE] “complete, up-to-date information about plan investment options” for all participants in self-directed plans. Since 1987, we have called upon the Labor Department to require all 401(k) investment products to give participants the same level of disclosure that ERISA and the securities laws require of mutual funds. Just last September, in testimony before the ERISA Advisory Council, ICI General Counsel Elizabeth Krentzman recommended requiring all 401(k) investment products to give participants a clear, concise statement of the key information they need. Under our proposal, this concise statement would be backed up with detailed information available online or in paper form upon request.

Our industry has been an advocate of better disclosure not just to 401(k) participants, but to plan sponsors as well. We have worked for more than a decade with others in the financial and benefits community to provide tools that can improve plan sponsors' understanding of fees and expenses, and how those expenses – for recordkeeping, investment management, and other services – are shared among 401(k) service providers.

Our industry's leaders recognize the significance of these issues. ICI's Board of Governors met last week, and one key item on its agenda was the consideration of a formal policy statement to reaffirm our commitment to meaningful disclosure in this area. The [statement adopted by our Board](#) signifies our industry's determination to help plan sponsors to make the right choices, and participants to make informed investment decisions. Once again, we are calling upon the Labor Department to ensure that sponsors and participants alike receive the information they need to fulfill their respective roles and responsibilities.

We need to ensure that all employers are equipped with basic information to understand three things:

- the total fees paid by the plan to all service providers;
- how expenses are allocated between the sponsor and participants, and
- any arrangements whereby a service provider receives some share of its revenue from a third party. Under ERISA, we believe, the obligation to provide this information should rest with those parties having a direct relationship with the employer.

For their part, participants need information on certain key features of their plans. The Labor Department should bring all investment options to the same standard by requiring each to provide a clear, concise statement covering five factors: investment objectives; principal risks; annual fees; historical performance, and the investment adviser that manages the product's investments.

The Pension Protection Act provides many new challenges for all of us engaged in the defined contribution retirement system. We in the mutual fund industry feel those challenges keenly. We have played a central role in the development of 401(k) plans, and we are proud of that role. Now, we must continue to innovate and expand the system to draw in more employers. We must continue to create incentives for more workers to participate – and provide high-quality investment options, education, and advice so that participants can make the best use of their savings opportunities.

You can be sure that ICI and our mutual fund members will continue to work with the Labor Department, with the Treasury Department and the Internal Revenue Service, with Congress, and with our partners in the private sector, to realize the full power of the Pension Protection Act and to strengthen working Americans' retirement security.

Thank you for your attention, and I hope you enjoy today's conference.

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