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Securities Industry Association
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April 1, 2004

Office of Regulations and Interpretations
Employee Benefits Security Administration
U.S. Department of Labor
200 Constitution Avenue, N.W., Room N-5669
Washington, D.C. 20210
Attn.: Automatic Rollover Regulation

Dear Sir or Madam:

On behalf of the Securities Industry Association's[1] Savings and Retirement Committee, I am writing to provide comments on proposed regulation section 2550.404a-2(c). The proposed regulation was issued in accordance with Section 657(a) of the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) which provides that if a plan makes a mandatory distribution of more than $1,000 but not exceeding $5,000, and the participant does not make an affirmative election to have the distribution rolled over or paid to him, the plan must automatically rollover the account to an Individual Retirement Account (IRA). The proposed regulations establish a safe harbor for plan fiduciaries of a pension plan that cause the rollover of an automatic distribution to an individual retirement plan. We appreciate the opportunity to comment on the proposed regulations but feel that certain revisions should be made to better serve the interests of all plan participants and IRA owners.

Imposition of below market rate fees

Proposed regulation section 2550.404a-2(c)(4)(ii) states that, "Fees and expenses attendant to the individual retirement plan may be charged only against the income earned by the

[1] The Securities Industry Association, established in 1972 through the merger of the Association of Stock Exchange Firms and the Investment Banker's Association, brings together the shared interests of nearly 600 securities firms to accomplish common goals. SIA member-firms (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. According to the Bureau of Labor Statistics, the U.S. securities industry employs 780,000 individuals. Industry personnel manage the accounts of nearly 93-million investors directly and indirectly through corporate, thrift, and pension plans. In 2003, the industry generated an estimated $209 billion in domestic revenue and $278 billion in global revenues. (More information about SIA is available on its home page: www.sia.com.)

individual retirement plan, with the exception of charges assessed for the establishment of the individual retirement plan." On a practical basis, these accounts will typically be quite small and by definition, unless they contain an earlier rollover distribution, cannot exceed $5,000 (the maximum automatic rollover permitted under section 401(a)(31)(B) of the Code). They will also be "problem accounts", i.e., statements will be frequently returned because the last known address from the plan administrator is not the current address, costs for forwarding mail and search efforts will be commonplace and as a consequence, tax reporting will be compromised.

We believe that it is unnecessarily restrictive to limit the fees that a regulated financial institution can charge after the establishment of the plan to the income earned by the plan, especially when the funds may only be invested in money market investments or similar investments, i.e., low-income generating investments. Since the proposed regulation provides that the fees cannot exceed the fees and expenses charged by the individual retirement plan provider for comparable individual retirement plans, a ceiling on fees is effectively imposed and it is one that will not be commercially viable.

This type of restriction on fees will mean that other investors or plan participants will subsidize the higher costs associated with these accounts. This indirect fee regulation discriminates against our clients who will eventually have to pay more to account for the losses that will be incurred in the increased costs of maintaining these accounts.

Section F of the Supplementary Information, the Department acknowledges that,

> "The proposal may affect the manner in which fees and expenses would otherwise have been allocated among plan sponsors and individual retirement plans. In some instances, particularly in the case of smaller individual retirement plans and when interest rates are low, the credited interest...may not cover the cost incurred by the provider to maintain the plan.... (I)ndividual retirement plan providers will offset or subsidize any such uncovered costs either through increased maintenance fees on larger automatic rollovers, through increased administrative charges to plan sponsors, or possibly both."

Notwithstanding this paragraph, there is no provision in the proposed regulation to charge an automatic rollover account a fee in excess of the annual income earned by the account, regardless of its size. Further, it is not realistic to expect that these lost fees will somehow be recaptured through increased maintenance fees or by charging increased administrative fees to plan sponsors. Service providers will readily attest to the fact that the retirement plan market is competitively priced. Organizations that do not offer automatic rollovers and do not have the need to subsidize losses on automatic rollovers will be able to gain a competitive edge in pricing.

Second, SIA is concerned that any attempt to offset the costs of an automatic rollover program by charging the plan administrator additional fees at the plan level could be deemed a violation of the Employee Retirement Income Security Act (ERISA) and the requirement to operate the plan for the exclusive benefit of the plan and the participants.

Third, the imposition of artificially discounted fees can be easily abused, even by automatic rollovers that are comprised, in part, of previous rollovers, without a predetermined date for the conversion of these rollovers to the regularly scheduled fees. Plan participants could view this as an opportunity to avoid paying individual retirement plan custodial fees indefinitely.

Fourth, by ignoring the notice provided by the plan administrator, participants can avoid the mandatory 20 percent withholding tax for distributions that would have been made directly to the participant, because they can withdraw funds from an IRA without incurring the 20 percent mandatory tax.

SIA recommends an approach that we believe is in the interests of **all** IRA account owners, plan sponsors, and defined contribution plan participants. We would suggest that the requirement to limit annual fees to available income be removed from the proposed safe harbor and replaced with language permitting fees to be charged for maintaining an automatic rollover that are comparable to IRAs with similar account balances. The proposed regulation provides that the fees cannot otherwise "exceed the fees and expenses charged by the individual retirement plan provider for comparable individual retirement plans ...that are not subject to the automatic rollover provisions ..." (Section 2550.404a-2(c)(4)(ii)), this should be sufficient to ensure that automatic rollover IRAs would not be subject to more fees than other IRAs with similar account balances.

Notice to participants

Section 2550.404a-2(c)(5) of the proposed regulation would require plan administrators to furnish participants with a summary plan description or summary of material modifications describing the provisions of the automatic rollover policy. SIA recommends instead that the notice be provided at the time of distribution. Notice provided in a plan description or modification may be received a couple of years before a participant is leaving the plan. In addition, the receiving financial institution may have changed in the interim. Finally, notifying all participants of the automatic rollover policy through a plan description of modification would be very costly to the plan administrator. Providing notice at the time of distribution would be more cost-effective and more participant-friendly.

Definition of "regulated financial institution"

The proposed regulation, in establishing a safe harbor for plan administrators seeking to cause the automatic rollover of a terminated participant's account balance, creates a "safe investment" corridor for the rollover, one that should create little or no risk to the participant and would therefore eliminate the fiduciary risk to the plan administrator. These investments "must be offered by a state or federally regulated institution as defined in paragraph (c)(3)(ii) of this section..." Paragraph (c)(3)(ii) provides that a regulated financial institution "shall be: a bank or savings association...an insurance company...or an investment company..." (proposed regulation section 2550.404a-2(c)(3)(i)). Brokerage firms are omitted from this definition, even though many are approved as non-bank trustees pursuant to Internal Revenue Code regulation section 1.408-2(e) and are also federally regulated institutions.

The overview of the proposal states that, "a bank, insurance company, financial institution or other provider of an individual retirement plan under the safe harbor is required to satisfy the requirements of the Code and the regulations issued thereunder. A footnote then references Internal Revenue Code regulation section 1.408-2(b)(2)(i) which provides that non-banks can be approved by the Internal Revenue Service to serve as trustees/ custodians of individual retirement accounts. Yet, these institutions are not included in the actual safe-harbor's definition of a "regulated financial institution". This discrepancy between the preamble and the text of the regulation will cause confusion in the marketplace. We would therefore recommend that proposed regulation section 2550.404a-2(c)(3)(ii) be revised to read, as follows, "For purposes of this section, a regulated financial institution shall be one that is state or federally regulated and that otherwise serves as trustee for individual retirement plans within the meaning of section 7701(a)(37) of the Code." This is a more inclusive term that includes banks or savings associations, credit unions, investment companies registered under the Investment Company Act of 1940, as well as brokerage firms that have been approved by the Internal Revenue Service as non-bank trustees and would serve to coordinate the description in the overview with the provision found in the proposed regulation.

Areas for further guidance

While the emphasis of the proposed regulation has been properly focused on the plan sponsor and the satisfaction of its fiduciary responsibility, individual retirement plan sponsors need to know if their policies and procedures comply with the requirements of the proposed regulation. The inclusion of several examples in the final regulations would provide sufficient guidance and would enable those sponsors to be able to inform plan fiduciaries that their automatic rollover individual retirement plan, available investments and procedures fall within the guidelines of the regulation.

The proposal acknowledges the need for additional guidance on some issues from the Internal Revenue Service (the "Service"). IRA providers face a number of significant legal impediments to establishing automatic rollover IRAs that require guidance to be issued from the Service before the Department issues final safe harbor guidance. We strongly recommend that the Department coordinate with the Service to ensure that the tax issues are addressed through the guidance process prior to the Department issuing final guidance. In addition, it will be particularly important for financial institutions to have guidance on compliance with the Patriot Act and escheatment issues before the regulation is finalized. In reference to the Patriot Act, SIA notes that the regulations issued under 31 CFR 103.122(a) (1)(ii) clarify that for purposes of the Patriot Act, plans under ERISA are not covered. The justification for this exemption is that the employer has already documented the individual's identity through the verification of a Social Security number and other identifiers. SIA believes this exemption should be applied to IRA rollover accounts as well. SIA members will need significant advance notice of the final regulation in order to implement the systems changes that will be necessary to implement these new requirements. We would respectively request a minimum of 6 months lead time before the final guidance becomes effective.

SIA appreciates this opportunity to comment on the proposed regulation and would be pleased to discuss the issues raised in this letter before a final regulation is issued. Please do not hesitate to call the committee's staff advisor, Liz Varley, at (202) 216-2000 if you would like to discuss these comments in further detail.

Very truly yours,

Laura Gough

Laura Gough
Chair
SIA Savings & Retirement Committee

cc: Ann Combs
Bob Doyle
Lou Campagna
Bill Sweetnam