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LAW OFFICES OF

DAVIS & HARMAN LLP

THE WILLARD

1455 PENNSYLVANIA AVENUE, N.W.

SUITE 1200

WASHINGTON, D.C. 20004

TEL (202) 347-2230

FAX (202) 393-3310

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Employee Benefits Security Administration
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Washington, DC 20210

To Whom It May Concern:

I am writing on behalf of a financial institution client active in the retirement services arena in response to the request for information ("RFI") published in the Federal Register on January 7, 2003, with respect to the automatic rollover provision enacted by section 657 of the Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA"). Under section 657 of EGTRRA, a plan that provides mandatory "cash-outs" of vested accrued benefits of greater than $1,000 is required to directly transfer such distributions to an IRA ("default IRA") unless the participant affirmatively elects to receive the distribution directly. Section 657 of EGTRRA directs the Department of Labor to issue safe harbors with respect to a plan sponsor's designation regarding the recipient institution for the default IRA and the initial investment of default IRA funds.

The RFI solicited public comment on a number of issues related to the automatic rollover provision and the development of safe harbors and regulations thereunder. The RFI states that the "Department also seeks information on low-cost individual retirement plans for transfers under [the automatic rollover provision]." This letter will focus on the portion of the RFI related to standards for safe harbor initial investments in default IRAs and will attempt to address the Department's interest in low-cost default IRA alternatives. In it, we make two central recommendations:

- First, that money market funds be designated by the Department as the primary or preferred safe harbor investment option for default IRAs; and

- Second, that if the Department should adopt an investment "mapping" approach as a safe harbor investment option that it not be designated as a preferred option.

As indicated, our first recommendation is that money market funds be designated as the primary or preferred safe harbor investment option for default IRAs. From the plan participant/default IRA owner's perspective, a money market investment would provide safety and ensure capital preservation – investment goals that are particularly well-suited to individuals with limited financial and retirement resources, as many default IRA owners will be. Equally important to these individuals, investment in a money market fund will substantially limit account costs and fees – another important goal when dealing with modest accounts of less than $5,000. Placement of default IRA assets in higher fee investment alternatives would absorb earnings in the accounts and expose the default IRA owner to a higher degree of investment risk. Moreover, in many instances there will be only a limited investment time horizon for the default IRA since individuals will often redeem account balances or rebalance investments once they become aware of the existence of the default IRA. In an investment vehicle with such a potentially short investment timeframe, a conservative money market fund that will preserve capital and guard against losses is the most appropriate investment option.

The lower relative costs associated with money market funds also make them an attractive safe harbor investment choice for default IRA providers. While default IRA providers laud the policy goal underlying the automatic rollover provision – preservation of retirement assets – they also confront the reality that they will lose money on these default IRA accounts in almost all instances. For example, the client on whose behalf this letter is written loses money on a typical IRA unless the account has a balance of at least $18,000. IRA providers generally are willing to absorb losses on smaller balance IRAs as a service to individual clients and also because of the potential to generate future revenue-earning business as the IRA balance grows. In contrast, default IRA owners (a number of whom are likely to be so-called lost participants with whom the plan sponsor cannot establish contact) may not even be aware of the service being provided. In addition, default IRA owners will often be of limited financial means and so will be less likely than the typical IRA holder to make significant additional contributions. For this reason, default IRA providers are likely to lose money over both the short-term and long-term on default IRA accounts they manage. While default IRA providers are committed to working with participants, plan sponsors, and federal policymakers to achieve the goals of the automatic rollover provision, they wish to do so in the most cost-effective way possible. Accordingly, default IRA providers' losses on these accounts should be minimized to the extent possible while still serving the policy goals underlying the provision. Designation of a money market fund as the primary safe harbor investment option would mitigate the financial burden imposed on the default IRA provider, and should be adopted as the Department's position in its automatic rollover guidance.

As part of the discussion over safe harbor investment alternatives, some have raised whether "mapping" of investment options under the employer-sponsored plan should be permitted as a default IRA safe harbor investment. From a cost perspective, such a mapping approach could be detrimental to plan participants. Under such an approach, the relatively small account balances in default IRAs would need to be divided into multiple, even smaller sub-accounts, with the attendant investment fees for each sub-account. From the perspective of the default IRA provider, the administrative costs associated with the mapping process and the maintenance of multiple sub-accounts would also be significant. An additional concern with the mapping approach would be how to handle situations where investment options comparable to those in the transferor employer plan are not available in the transferee default IRA. For these reasons, should the Department include mapping as a suitable safe harbor investment alternative, we strongly urge that it merely be one of a number of permissible alternatives and not be designated as a preferred option.

In conclusion, we urge you to specify money market funds as a primary safe harbor investment option for default IRAs established pursuant to section 657 of EGTRRA. Money market funds are an optimal investment option because they reduce costs both for default IRA owners and default IRA providers. At the same time, money market funds provide safety and capital preservation. For the reasons stated above, we also urge you to avoid designating a mapping approach as a required or preferred safe harbor investment alternative.

If you have any questions or if I can provide any additional information, please do not hesitate to contact me at (202) 662-2294.

Sincerely,

James M. Delaplane, Jr