INVESTMENT COMPANY INSTITUTE

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**COMMENT LETTER**

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# ICI Comment Letter on EC Consultation on the Modernization of European Pension Systems (pdf)

November 15, 2010 European Commission Directorate-General for Employment, Social Affairs & Equal Opportunities Green Paper on Pensions Consultation, Unit E4 Rue Joseph II Office J-27 1/216 B – 1040 Brussels Re: European Commission Green Paper: Towards Adequate, Sustainable and Safe European Pension Systems Dear Sirs: The Investment Company Institute1 strongly supports the European Commission's efforts to launch a European dialogue on the key challenges facing pension systems and how the European Union ("EU") can support Member State efforts to deliver adequate and sustainable pensions.2 We agree that pension systems that enable individuals to maintain, to a reasonable degree, their living standard after retirement are crucial for citizens. While challenges to creating an appropriate system are great, we believe they can be met. We also believe the retirement savings framework in the United States provides some useful insights as you consider reform of EU pension systems. Like the EU, the United States continues to examine ways to strengthen our own retirement system to ensure that it affords adequate financial security to US citizens in retirement. The basic framework for private-sector plans was enacted with the Employee Retirement Income Security Act of 1 The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of $12.05 trillion and serve over 90 million shareholders. 2 European Commission, Green Paper: Towards Adequate, Sustainable, and Safe European Pension Systems, dated July 7, 2010 (the "Green Paper"), available at http://ec.europa.eu/social/main.jsp?langId=en&catId=89&newsId=839&furtherNews=yes. European Commission November 15, 2010 Page 2 of 15 1974 ("ERISA") and updated with the Pension Protection Act ("PPA") in 2006 to strengthen funding of defined benefit plans and better meet the needs of defined contribution ("DC") plans. In the United States, national policies for DC plans have proven integral to helping Americans prepare for retirement. Because mutual funds manage almost half of the assets in DC plans and individual retirement accounts ("IRAs"),3 the Institute has devoted considerable resources to studying the US retirement system and participants' activities. Mutual funds are the investment of choice in DC plans because they offer easy access to professional investment management and diversification in a highly regulated and transparent product with strong investor protections. Therefore, we greatly value the opportunity to offer constructive input as the EU explores ways to strengthen retirement security. The US DC system of 401(k) and similar plans has been a huge success.4 DC plan assets are a significant component of Americans' retirement assets, representing about one-quarter of the total retirement market and almost one-tenth of US households' aggregate financial assets in the second quarter of 2010.5 As of mid-2010, Americans had saved $4.0 trillion in DC plans, and another $4.2 trillion in IRAs.6 The success of the DC plan system is evidenced by wide employer adoption and worker participation, as well as participant feedback and research showing the capability of DC plans to provide significant retirement income. In 2007 (the latest official data), there were 658,805 private- 3

For complete data on the US retirement market through the second quarter of 2010, see Brady, Holden, and Short, The U.S. Retirement Market, Second Quarter 2010, ICI Fundamentals, vol. 19, no. 3-Q2 (October 2010), available at www.ici.org/pdf/fm-v19n3-q2.pdf ("U.S. Retirement Market, Second Quarter 2010"). 4 Employer-sponsored DC plans provide employees with an account derived from employer contributions or employee deferrals of earnings, or both, plus any investment earnings or losses on those contributions. Introduced through IRS regulations in 1981, 401(k) plans have grown to become the most common employer-sponsored DC plan in the United States. Other types of employer-sponsored DC plans include 403(b) plans (available to employees of schools and non- profits), 457 plans (offered primarily to government employees), and Keoghs (for the self-employed). For detailed information on 401(k) plans and their history, see Holden, Brady and Hadley, 401(k) Plans: A 25-Year Retrospective, ICI Perspective, vol. 12, no. 2 (November 2006), available at www.ici.org/pdf/per12-02.pdf. See also, 2010 Investment Company Fact Book ("2010 Fact Book"), Chapter 7, available at www.icifactbook.org/, for a discussion of the role of mutual funds in retirement savings; and U.S. Retirement Market, Second Quarter 2010 for retirement market data through the second quarter of 2010. 5 See Holden, Defined Contribution Plan Participants' Activities: First Half 2010, Investment Company Institute, available at www.ici.org/pdf/ppr_10_rec_survey-q2.pdf ("DC Plans: First Half 2010"). 6 See U.S. Retirement Market, Second Quarter 2010. Estimates suggest about half of all IRA assets originated in 401(k) and other employer-sponsored plans and were then rolled over to IRAs.  sector DC plans with 66.9 million active participants.7 Institute research from late 2009 - during the recent financial downturn - shows that Americans have confidence in 401(k) plans and support their basic features. In particular, the survey research shows high levels of support for: individual choice and control of their investments in retirement accounts; convenience of payroll deduction; and tax-favored savings. Importantly, 73 percent of all households are "somewhat confident" or "very confident" that 401(k) plans and similar retirement plans can help Americans meet their retirement goals.8 Although the Green Paper does not offer specific reforms, several important issues are set forth for discussion. We describe below how the US retirement savings framework has sought to address the following issues raised in the Green Paper: • Ensuring adequate income and long-term sustainability of pensions; • Stability in the wake of financial market downturns; • Transparency and facilitating informed decisions; and • Removing cross-border obstacles or portability of retirement savings. We hope that you find this information useful in your consideration of EU pension reform. I. Ensuring Adequate and Sustainable Pensions A. Defined Contribution Plans Can Provide Significant Retirement Income The Green Paper states that one of the overarching objectives of pension reforms in the EU is to ensure that pension systems are adequate. For many American workers, DC plan accounts have become an important part of their retirement planning. While there is some disagreement in the United States on whether Americans are saving enough for retirement in DC plans, Institute research

7 See U. S. Department of Labor, Employee Benefits

Security Administration, Private Pension Plan Bulletin Historical Tables and Graphs (2007 Data Release Version 1.3), U.S. Department of Labor (June 2010), available at www.dol.gov/ebsa/pdf/1975-2007historicaltables.pdf. The bulk of these plans were 401(k) plans, with 490,917 plans and 59.6 million active participants. 8 See Holden, Sabelhaus, and Reid, Enduring Confidence in the 401(k) System: Investor Attitudes and Actions, Investment Company Institute (January 2010), available at www.ici.org/pdf/ppr_10_ret_saving.pdf ("Enduring Confidence in the 401(k) System"). European Commission November 15, 2010 Page 4 of 15 demonstrates that DC plans can play a critical role in supplementing retirement income from other sources and that DC plans, ultimately, can provide significant retirement income.9 It is important not to judge the success of the 401(k) system by the current size of account balances because the 401(k) system is new enough so that no one has yet had a full career in the system. In addition, looking at individual account balances is potentially misleading because it is common for workers to have several jobs, in each of which the worker has a 401(k) or similar account. Further, private-sector plan accumulations need to be considered together with benefits provided to all workers by the government, particularly, Social Security in the United States, which provides workers with a baseline annuity benefit. To help get an understanding of whether a full career with 401(k) plans can produce adequate income replacement rates at retirement, the Institute, in collaboration with the Employee Benefit Research Institute ("EBRI"), created the EBRI/ICI 401(k) Accumulation Projection Model. This model examines how 401(k) accumulations might contribute to future retirees' income based on decisions workers make throughout their careers. The model looks at 401(k) participants of varying income levels and models future accumulations under a range of participant behaviors and scenarios— including modeling various long-term market returns that included significant historical market downturns. The model demonstrates that 401(k) plans can produce adequate replacement rates at retirement when combined with Social Security.10 For example, among individuals who were in their late twenties in 2000, after a full career with 401(k) plans, the median individual in the lowest income quartile is projected to replace about 100 percent of his or her pre-retirement income at age 65 using 9 See Holden and VanDerhei, Can 401(k) Accumulations Generate Significant Income for Future Retirees? and The Influence of Automatic Enrollment, Catch-Up, and IRA Contributions on 401(k) Accumulations at Retirement, ICI Perspective and EBRI Issue Brief, Investment Company Institute and Employee Benefit Research Institute, November 2002 and July 2005, respectively, available at www.ici.org/pdf/per08-03.pdf ("Can 401(k) Accumulations Generate Significant Income") and www.ici.org/pdf/per11-02.pdf ("The Influence of Automatic Enrollment"), respectively. 10 The United States has a system of regular retirement income funded by taxes—Social Security—and one of the most crucial tasks in addressing retirement security in the future is ensuring that Social Security continues to provide monthly benefits to retired and disabled workers. Workers with low to moderate lifetime earnings have historically replaced most of their pre-retirement earnings through Social Security, and barring policy changes that would make the system much less progressive, will continue to do so in the future. For a discussion of Social Security replacement rates, see Congressional Budget Office, CBO's Long-Term Projections for Social Security: Additional Information, Congressional Budget Office (October 2010), available at www.cbo.gov/ftpdocs/119xx/doc11943/10-22-SocialSecurity_chartbook.pdf. European Commission November 15, 2010 Page 5 of 15 401(k) accumulations and Social Security.11 The model also demonstrates that when workers move into jobs that do not offer 401(k) plans, median replacement rates fall significantly – by more than half for workers in the lowest income quartile. Other research demonstrates that, once Social Security, savings during employment, and taxes are accounted for, even moderate savings rates can lead to adequate replacement rates after retirement.12 B. Plan Design Features Can Increase Retirement Accumulations Automatic enrollment is one mechanism found to increase retirement accumulations in the United States. Originally it was typical for employers offering 401(k) plans to ask employees to sign up for the plans. In plans with an automatic enrollment feature, workers are notified they will be automatically enrolled in the plan, and have contributions of a specified amount deducted from their pay and invested in the plan's default investment unless they opt out of the plan or select a different investment. Research shows that, in the United States, automatic enrollment increases plan participation and savings rates (particularly among lower-income workers), and that the selection of a default investment that includes equity exposure positively impacts account balances over a worker's career.13 While automatic enrollment has been a permissible plan design feature in the United States for many years, Congress included provisions in the PPA to encourage employers to adopt automatic enrollment by, among other things, providing fiduciary relief for employers using qualified default

11 The EBRI/ICI 401(k) Accumulation Projection Model forecasts replacement rates at age 65 for a cohort of 401(k) participants turning 65 between 2030 and 2039. For details, see Can 401(k) Accumulations Generate Significant Income and The Influence of Automatic Enrollment. 12 See Peter J. Brady, "Measuring Retirement Resource Adequacy," Journal of Pension Economics and Finance (Vol. 9, No. 2 (April 2010); "Can 401(k) Plans Provide Adequate Retirement Resources?" Pension Research Council Working Paper, PRC WP 2009-01; and "What Does the Market Crash Mean for the Ability of 401(k) Plans to Provide Retirement Income?" National Tax Journal, Vol. LXII, No. 3 (September 2009). 13 See The Influence of Automatic Enrollment; James J. Choi, David Laibson, Brigitte C. Madrian, and Andrew Metrick (2004), "Saving For Retirement on the Path of Least Resistance," originally prepared for Tax Policy and the Economy 2001, updated draft: July 19, 2004; James J. Choi, David Laibson, Brigitte Madrian, and Andrew Metrick (2002), "For Better or For Worse: Default Effects and 401(k) Savings Behavior," Pension Research Council Working Paper, PRC WP 2002-2; and Brigitte C. Madrian and Dennis F. Shea (2001), The Power of Suggestion: Inertia in 401(k) Participation and Savings Behavior," The Quarterly Journal of Economics, Vol. CXVI, Issue 4, November 2001: pp. 1149–1187; and The Vanguard Group, How America Saves 2010: A Report on Vanguard 2009 Defined Contribution Plan Data, The Vanguard Group, Vanguard Center for Retirement Research (2010), available at https://institutional.vanguard.com/iam/pdf/HAS.pdf ("Vanguard 2009 DC Plan Data").



investment options. Since passage of the PPA, employers have adopted automatic enrollment at a rapid pace. Vanguard reports that for DC plans it services, 21 percent of plans used automatic enrollment in 2009, up from just 5 percent in 2005. Among the largest plans (more than 5,000 participants), 43 percent used automatic enrollment in 2009.14 Under US law, in automatic-enrollment plans and other contexts where a participant fails to give investment direction, the employer must specify the vehicle into which the contributions will be invested (the "default investment"). Employers generally may designate any type of default investment, provided that the choice is an appropriate retirement savings investment, and not merely a holding place for the employee's funds (i.e., diversified and containing a mix of asset classes providing capital appreciation and preservation). US public policy is that participants defaulted into an investment option should benefit from exposure to the equity markets for long-term retirement savings.15 II. DC Plans Can Provide Financial Stability in the Wake of Financial Market Downturns Financial markets in the United States and around the world experienced unprecedented turmoil in the past few years. The Green Paper appropriately recognizes that this turmoil has had and will continue to have a significant impact on the pensions of EU citizens, and that there is a need to consider the regulation of funded pension schemes in the wake of this financial turmoil. During the height of the financial turmoil, a few critics in the United States claimed that the DC system was seriously flawed and advocated replacing it with a mandatory government-provided system. Institute research consistently demonstrates, however, that the US DC system stands on solid footing and can withstand financial shock. Plan investors can withstand market volatility, consistent 401(k) contributors have seen their accounts rebound after bear markets, and plan investors have demonstrated a commitment to long-term savings.16 We firmly believe that it would be a mistake to use recent market events as a reason to discourage the development of DC schemes.

14 See Vanguard 2009 DC Plan Data. 15 See 72 Fed. Reg. 60451 at 60463 ("It is the view of the Department of Labor that investments [for] defaulted participants ought to and often will be long-term investments and investment…in money market funds or stable value funds will not over the long-term produce rates of return as those generated by [qualified default investment alternatives], thereby decreasing the likelihood that participants invested in capital preservation products will have adequate retirement savings."); and Institute Letter to Department of Labor, dated Nov. 13, 2006, available at www.ici.org/pdf/20574.pdf. 16 See Statement of the Investment Company Institute at the Hearing on "The Impact of the Financial Crisis on Workers' Retirement Security" Before the House Education and Labor Committee (October 21, 2008) ("October 2008 Testimony"), available at http://www.ici.org/pdf/23010.pdf. European Commission November 15, 2010 Page 7 of 15 A. Long-Term Retirement Investors Do Not Overreact and Can Withstand Market Volatility The Institute has long found that mutual fund investors do not overreact to market volatility. The Institute has also analyzed the behavior of 401(k) plan participants and found that they make few changes in their accounts and benefit from dollar cost averaging as they contribute paycheck-by- paycheck. In the mid-1990s, the Institute analyzed mutual fund shareholder activity during the 14 major stock market cycles going back to World War II.17 In none of the stock market breaks and sharp declines did mutual fund investors liquidate their shares en masse.18 This was seen even in the aftermath of the October 19, 1987 market crash: only about 5 percent of stock fund shareholders liquidated shares in the six weeks after the crash. Analysis of the 1987 market break showed that it was chiefly institutional investors, and not individuals in retail accounts, 401(k)s or IRAs, that drove the market down.19 The 95 percent of mutual fund shareholders who did not liquidate mutual fund shares in the six weeks after the October 19, 1987 market crash were poised to benefit from the market rebound that followed October 1987. B. Rebound in Participant 401(k) Accounts The ability to recover from market downturns is also seen in the experience of individual 401(k) accounts. The EBRI/ICI Participant-Directed Retirement Plan Database, the largest, most representative repository of information about individual 401(k) accounts, shows that participants who stay in the system and continue saving see their accounts rebound significantly.20 For example, an

17 See Rea and Marcis, Mutual Fund Shareholder Activity During U.S. Stock Market Cycles, 1944–95, ICI Perspective, vol. 2, no. 2 (March 1996), available at http://www.ici.org/pdf/per02-02.pdf. 18 The research found that mutual fund investors are not insensitive to stock price movements, but their response tends to be spread over time, and tends to be in response to long-run trends in equity returns. Subsequent research shows that mutual fund shareholders' reaction to significant downturns or major events, such as the September 11, 2001 attacks, is muted. See Reid, Millar, and Sevigny, Mutual Fund Industry Developments in 2001, ICI Perspective, vol. 8, no. 1 (February 2002), available at http://www.ici.org/pdf/per08-01.pdf. The Institute also looked at net flows of funds during the period between June 2002 and February 2003, when the stock market fell 21 percent, and found equity funds had outflows of only 3.3 percent of assets held in equity funds at the beginning of the decline. 19 See testimony of Nicholas Brady, Chairman, Presidential Task Force on Market Mechanism, Hearings before the

Committee on Banking, Housing, and Urban Affairs, U.S. Senate (Feb. 2, 3, 4, and 5, 1988), S. Hrg. 100-649, page 52. 20 The Employee Benefit Research Institute (EBRI) and the Institute collaborate on an annual 401(k) data collection project. For the most recent update from the project, see Holden, VanDerhei, and Alonso, 401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2008, ICI Perspective, Vol. 15, No. 2, and EBRI Issue Brief, No. 335, Investment European Commission November 15, 2010 Page 8 of 15 analysis of participants with account balances at the end of each year from 1999 through 2006 (that is, consistent savers in the database) shows that between 1999 and 2002, the average account balance of this group fell 8 percent.21 But in 2003 the average account balance was up 30 percent. The average account balance almost doubled from the bottom (2002) through 2006. Overall, the average account balance from 1999 to 2006 was up 79 percent, despite the multi-year bear market and even though US equity prices had not recaptured all their losses during the 2000–2002 market downturn. If those participants had stopped contributing, left the 401(k) system or moved their balances out of the stock market in 2002, they would have locked in their losses and missed the market rebound.22 Ongoing contributions and asset diversification muted the impact of the 2008 market downturn on 401(k) accounts. Analysis of another group of consistent 401(k) participants—those who stayed in their plans from year-end 2003 through year-end 2008—finds that the average 401(k) account balance moved up and down with stock market performance, but over the entire five-year time period increased at an average annual growth rate of 7.2 percent.23 We know from history that staying the course prevents savers from locking in their losses and missing the market rebound. Even those close to retirement can see their accounts come back because savers typically do not spend their entire account right away at retirement.24 Just as importantly, participants in 401(k) and other DC plans have the advantage of regular contributions by payroll deduction, through good and bad markets, which allows them to take advantage of dollar cost averaging—buying more when market prices are depressed.

Company Institute and Employee Benefit Research Institute (October 2009), available at www.ici.org/pdf/per15-02.pdf ("401(k) Plans - 2008"). 21 See Holden, VanDerhei, Alonso, and Copeland, 401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2006, ICI Perspective, vol. 13, no. 1, and EBRI Issue Brief, No. 308, Investment Company Institute and Employee Benefit Research Institute (August 2007), available at www.ici.org/pdf/per13-01.pdf. 22 For an analysis of the group of consistent 401(k) participants present from year-end 1999 through year-end 2007, see Holden, VanDerhei, and Alonso, What Does Consistent Participation in 401(k) Plans Generate?, ICI Perspective, Vol. 15, No. 1, and EBRI Issue Brief, No. No. 332-SR, Investment Company Institute and Employee Benefit Research Institute (July 2009), available at www.ici.org/pdf/per15-01.pdf. From year-end 1999 through year-end 2007, the average 401(k) account balance among consistent participants increased at an average growth rate of 9.5 percent per year. 23 See 401(k) Plans – 2008. 24 For research on defined contribution plan–owning households' decisions surrounding the disposition of their DC plan balances at retirement, see Sabelhaus, Bogdan, and Holden, Defined Contribution Plan Distribution Choices at Retirement: A Survey of Employees Retiring Between 2002 and 2007, ICI Research Series (Fall 2008), available at www.ici.org/pdf/rpt_08_dcdd.pdf ("DC Plan Distribution Choices at Retirement"). European Commission November 15, 2010 Page 9 of 15 C. Demonstrated Commitment to Long-Term Savings While some news reports suggest that US investors reacted to the recession by tapping their workplace retirement accounts, reducing or stopping contributions, or changing how their existing balances or new contributions are invested – that is not the case. DC plan participants have not raided their nest eggs. The withdrawal and contribution data from a recent Institute survey of a cross-section of recordkeepers indicate that most DC plan participants continued to participate in their retirement plans at work.25 In 2009, only 3.1 percent of plan participants had taken withdrawals from their DC plans, with 1.6 percent taking hardship withdrawals. This level of withdrawal activity is in line with past years' experiences among the recordkeepers, and is consistent with the rate of withdrawal activity observed in the EBRI/ICI 401(k) database in 2000 (at the beginning of the 2000–2002 bear market in equities).26 The Institute's survey similarly found that loan activity remained in line with the experience of the past several years. Indeed, surveys of retirement savers find most leave their money invested in a 401(k) plan or IRA until the government forces them to begin removing it at age 70½.27 Retirement savers also appear to continue to save even during bear markets. Just as few participants have tapped their DC plan accounts during the past two years, few participants have stopped contributing to them. Although there is concern that plan participants might stop devoting some of their paychecks to retirement saving during times of financial stress, recordkeepers indicate that only 3.4 percent of plan participants stopped making contributions in 2009.28 An analysis of a large sample of 401(k) participants drawn from the EBRI/ICI database, which includes data for the 2000–

25 See Enduring Confidence in the 401(k) System; and DC Plans: First Half 2010. For earlier survey results, see Holden and Reid, Retirement Saving in Wake of Financial Market Volatility, Investment Company Institute (December 2008), available at www.ici.org/pdf/ppr_08_ret_saving.pdf. 26 Analysis of the 2000 EBRI/ICI 401(k) database found that 4.5 percent of active 401(k) plan participants had taken in-service withdrawals, including hardship withdrawals. Withdrawal activity varied with participant age; participants younger than 60 were much less likely to take a withdrawal compared with participants in their sixties. See Can 401(k) Accumulations Generate Significant Income. 27 See DC Plan Distribution Choices at Retirement. In addition, among traditional IRA–owning households making withdrawals, the most commonly cited reason is to meet required minimum distributions. See Holden and Schrass, The Role of IRAs in U.S. Households' Saving for Retirement, 2009, ICI Fundamentals, vol. 19, No. 1 (January 2010), available at www.ici.org/pdf/fm-v19n1.pdf. 28 See DC Plans: First Half 2010.  2002 market downturn, also found that contribution rates were little changed in 2000, 2001, or 2002, compared to 1999.29 III. Transparency and Facilitating Informed Decisions A. Participants and Plan Sponsors Need Meaningful and Effective Disclosure In the United States, participants are allowed to direct the investment of their retirement accounts, and the U.S. Department of Labor ("DOL") requires that plan sponsors offer at least three investment options covering a range of risk and return. Plan sponsors are fiduciaries under ERISA and, as such, must act solely in the interest of plan participants, including with respect to the selection of investment options. As the Green Paper recognizes, when the choice and responsibility of selecting investments for retirement accounts are placed on individuals, they must be provided with appropriate information regarding the products in which they can invest. And when employers enter into arrangements with firms for recordkeeping plan accounts or when they select the investments the plan will offer to participants, they need relevant information for making those decisions. Providing meaningful and effective disclosure to DC plan participants and employers is fundamental to developing and enhancing DC plans.30 In the United States, regulators recently revised their rules to set out in greater detail the information that must be provided about all plan investment options. In the Institute's view, disclosure requirements should be based on the following principles. Participant-Level Fee Disclosure. Participants need simple, straightforward disclosure on all investment products offered in a plan focused on the key information that allows comparisons among the investment options available in their plan. Voluminous and detailed disclosure will not serve the interests of participants, whose primary decisions are whether to participate in the plan (and at what

29 See Holden and VanDerhei, “Contribution Behavior of 401(k) Plan Participants During Bull and Bear Markets,” National Tax Association Proceedings, Ninety-Sixth Annual Conference on Taxation, November 13-15, 2003, Chicago, Illinois, pp. 44-53, National Tax Association (2004). 30 Meaningful and effective disclosure to 401(k) plan participants and employers and has long been an Institute priority. See, e.g., Investment Company Institute comment letter on Participant Fee Disclosure Project (Sept. 8, 2008), available at www.ici.org/statements/cmltr/08_dol_401k_disclosure_com.html; and Testimony of Paul Schott Stevens President and CEO Investment Company Institute on “Strengthening Worker Retirement Security” Hearing Before the Education and Labor Committee U.S. House of Representatives (February 24, 2009) (“February 2009 Testimony”), available at www.ici.org/govaffairs/testimony/09_house_401k_tmny.  level) and how to allocate their accounts among the options the plan sponsor has selected. The best disclosure approach is one that is layered to deliver the right level of information based on participants’ actual needs31 — key information on every investment option provided to all upon enrollment, and more detailed information available to all online and in paper form upon request. Disclosure that is focused and useful to participants serves an important role in helping workers be better savers and better investors. The new participant disclosure rule adopted by the DOL sets out the investment information to be provided to 401(k) plan participants.32 The rule imposes new disclosure requirements with respect to all investment options, not just mutual funds, which the Institute believes is essential to an effective disclosure structure. Disclosure to Plan Fiduciaries. Disclosure by service providers to plan sponsors (employers) should provide information that allows them to fulfill their fiduciary responsibility, including selecting and monitoring service providers and reviewing the reasonableness of plan fees.33 In particular, plan sponsors should obtain information from service providers on the services that will be delivered, the fees that will be charged, and whether and to what extent the service provider receives compensation from other parties in connection with providing services to the plan. The new rule governing disclosure by service providers sets out the information to be provided to plan fiduciaries.34 The regulation requires plan recordkeepers and other service providers to give employers comprehensive information on the aggregate compensation they receive before a contract is entered into, and on an ongoing basis thereafter. This includes information on direct payments from 401(k) plans to recordkeepers and payments from third parties. When recordkeepers make available a

31 After years of effort, the U. S. Securities and Exchange Commission recently completed a widely-praised overhaul of mutual fund prospectus requirements, which allows funds to provide investors a “summary” prospectus that all investors receive, with the full statutory prospectus available online or in paper upon request. See Enhanced Disclosure and New Prospectus Delivery Option for Registered Open-End Management Investment Companies, 74 Fed. Reg. 4546 (Jan. 26, 2009). This lengthy process has immediate relevance to 401(k) disclosure efforts. 32 29 C.F.R. § 2550.404a-5. 33 See Statement of the Investment Company Institute to ERISA Advisory Council Working Group on Fiduciary Responsibilities and Revenue Sharing Practices (September 20, 2007), available at www.ici.org/statements/tmny/07_dol_disclose_tmny.html; and Statement of the Investment Company Institute to ERISA Advisory Council Working Groups on Disclosure (September 21, 2004), available at www.ici.org/statements/tmny/04_dol_krentzman_tmny.html. 34 29 C.F.R. § 2550.408b-2.  platform of investments from which plan fiduciaries can select the investments the plan will offer, the new rule requires the recordkeeper also to provide key information about the investments used in the plan, including fund expense ratios, and any charges to buy or sell the

investment. B. DC Plan Participants Make Responsible Investment Choices When Provided Appropriate Tools The Green Paper expresses concern about the ability of plan participants to bear the risks involved in selecting investments for their own accounts. The US experience indicates that plan sponsors and service providers are committed to providing information, education and tools to participants to assist them and research shows that participants generally make appropriate investment decisions. The retirement industry has worked hard to develop innovative and interactive tools to help explain investing concepts and has introduced state of the art ways to communicate with and assist participants. DC plan participants now have access to sophisticated call centers, websites, educational materials, and access to professional investment managers — high-touch ways for participants to receive information about their accounts. The industry also has developed new products geared to retirement savings, such as target date funds. Target date funds, which are also called lifecycle funds, are designed to offer a convenient and efficient way to invest for a person expecting to retire around a particular date. A target date fund pursues a long-term investment strategy, using a mix of asset classes (or asset allocation). A target date fund typically rebalances its portfolio to become less focused on growth and more focused on income as it approaches and passes the target date of the fund, which is usually included in the fund's name.35 Fund providers typically offer target date funds with target dates spaced at five or ten-year intervals to meet the needs of retirement investors across a wide range of ages.36 Over the past several years, target date funds have been increasingly offered in DC plans and participants have increasingly invested in them. As of the end of June 2010, target date mutual funds had $270 billion in assets, including $168 billion held in DC plans, and another $50 billion held in IRAs.37 In 401(k) plans that offer target date 35 Research shows that asset allocation is one of the most important factors in long-term portfolio performance. Further, research shows that, left to their own direction, some young workers invest very conservatively, by allocating all, or almost all, of their accounts to fixed-income investments, while some participants nearing retirement invest very aggressively, allocating all, or almost all, of their accounts to equity investments. See 401(k) Plans – 2008. 36 For example, an individual anticipating retirement in 2039 could invest in a 2040 fund, while one expecting to retire in 2012 might choose between a 2010 fund and a 2015 fund. For additional information on target date funds, see the Institute's resource page on target date funds, available at www.ici.org/trdf. 37 See The U.S. Retirement Market, Second Quarter 2010. European Commission November 15, 2010 Page 13 of 15 funds, 42 percent of participants had at least some portion of their account in these funds.38 To put these statistics in perspective, about 7 percent of total assets in 401(k) plans in the EBRI/ICI 401(k) database were in target date funds at the end of 2008. In the retirement industry, providers compete on the quality and level of services provided to participants. The result is that DC plan investors receive information and guidance to make appropriate investment decisions. The Institute believes a DC plan system should not dictate the investment or distribution line-up of plans, or try to legislate their risk characteristics or prescribe approaches to asset allocation. All of these are tasks for which regulators are unsuited and should be left to the conscientious oversight of plan sponsors. Specifically, we believe that the government should not mandate that all plans offer any particular investment. Regulators should not endorse one investment strategy over another or get in the business of deciding what types of investments should be in plan investment lineups, particularly when there is no indication that plan sponsors cannot make prudent judgments in selecting plan investment menus.39 Investors agree. In fact, almost nine in ten US households surveyed rejected the idea that the US government, and not individuals, should make investment decisions for retirement accounts.40 Collaborative research between the EBRI and the Institute demonstrates that participants generally make sensible choices in allocating their investments while accumulating assets in their 401(k) plans. For example, at year-end 2008, individuals in their 20s held 46 percent of their accounts in equity funds and company stock; 28 percent in lifecycle funds and non-lifecycle balanced funds; and only 23 percent in guaranteed investment contracts, stable value funds, money funds, and bond funds. By comparison, individuals in their 60s allocated 36 percent of their assets in equity securities; 14 percent in lifecycle and non-lifecycle balanced funds; and 47 percent in fixed-income securities.41

38 See 401(k) Plans- 2008. In the EBRI/ICI 401(k) database, target date funds include mutual funds, collective investment trusts, and separately managed accounts. 39 See February 2009 Testimony. 40 This result was first found in the Institute's survey of 3,000 US households in late October through December 2008— that is, during some of the most jarring days in the history of our financial markets (see Holden and Reid, Retirement Saving in Wake of Financial Market Volatility, Investment Company Institute (Dec. 2008), available at www.ici.org/pdf/ppr_08_ret_saving.pdf). ICI surveyed 3,000 US households in late November 2009 through December 2009 and found similar results (see Enduring Confidence in the 401(k) System). 41 See 2010 Fact Book at 104. European Commission November 15, 2010 Page 14 of 15 Institute research shows that investors in DC plans and IRAs also make sensible choices in retirement. Extensive research by the Institute shows that, by and large, people act responsibly with their DC plan account balances at retirement and are responsible stewards of their IRA assets (which often contain significant rollover amounts from employment-based plans).42 In fact, retirees tend to preserve these accounts in retirement until the government forces a distribution.43 A survey the Institute conducted in 2007 of recent retirees about how they used their DC account proceeds at retirement showed that respondents pursued a range of outcomes reflecting their own personal needs, in many cases rolling some or all of their account balances over to IRAs.44 In making their distribution decision, retirees with a choice of options often consulted multiple sources of information. Forty-two percent indicated they sought advice from a professional financial adviser they found on their own.45 IV. Removing Cross-Border Obstacles or Portability The Green Paper states that EU pension reforms should consider, and not hinder, the mobility of labor and capital. DC plans are uniquely suited for a mobile work force. They can afford workers the opportunity to accumulate retirement assets at each job and to remain invested in their retirement contributions after leaving a job. US law imposes tax penalties on workers who cash out their retirement accounts when leaving a job and do not leave the money in the plan or roll it into an IRA. DC plans are required to offer participants the option to have distributions directly rolled over to an IRA or another employer's plan.46 To encourage participants to have distributions rolled over to an IRA or another employer's

42 See Holden and Schrass, The Role of IRAs in U.S. Households' Savings for Retirement, 2009, ICI Fundamentals, vol. 19, no. 1 (January 2010), available at www.ici.org/pdf/fm-v19n1.pdf ("The Role of IRAs"); and DC Plan Distribution Choices at Retirement. 43 Sixty-one percent of traditional IRA–owning households not making withdrawals in tax year 2007 indicated it was unlikely they would withdraw from their IRAs before age 70½. Slightly more than half of traditional IRA–owning households without withdrawals indicated a future use of the monies would be to cover an emergency, such as healthcare expenses. See February 2009 Testimony. Similar results occur in more recent years; for example, see the 2009 ICI IRA Owners Survey results in The Role of IRAs. 44 DC Plan Distribution Choices at Retirement. 45 DC Plan Distribution Choices at Retirement. 46 26 U.S.C. 401(a)(31). European Commission November 15, 2010 Page 15 of 15 plan, regulations require a 20 percent withholding on a distribution eligible to be rolled over that is paid to the participant.47 * * * * * We appreciate the opportunity to express our views on the Green Paper. We hope that the information provided by the Institute will be useful as the Commission considers EU pension reform. If you have questions or if we can

provide any additional information, please feel free to contact me at solson@ici.org or +1-202-326-5813. Sincerely, /s/ Susan M. Olson Susan M. Olson Senior Counsel – International Affairs 47 26 U.S.C. § 3405.