the safety available insurance carrier when choosing an annuity provider. Cases have been brought against several companies which purchased annuities from Executive Life including Pacific Lumber Co., Magnetek, Inc., Smith International, Inc., Geosource, Inc., American National Can Company, AFG Industries, Inc., and Raymark Industries, Inc. as well as against the Strouse Adler Company which purchased annuities from Presidential Life Insurance Company. It is the Department's position that these fiduciaries breached their fiduciary responsibilities under ERISA in connection with their selection of annuity providers.⁴ Consent orders settling the Secretary's claims have been entered in certain of these cases.

Regulatory Action

In addition to its enforcement activities, the Department and the Pension Benefit Guaranty Corporation (PBGC) sought to determine if, in addition to and independent of ERISA's fiduciary standards, minimum standards for annuity providers would be appropriate and necessary in order to ensure a reasonable likelihood that participants or beneficiaries on whose behalf annuities are purchased will receive their promised pension benefits. It was anticipated that such modification might be effected by amending the minimum standards which already exist under the regulation at 29 CFR 2510.3-3(d)(2)(ii). On June 21, 1991, both the Department and the PBGC published advanced notices of proposed rulemaking (ANPRMs) in the Federal Register (56 FR 28638 and 56 FR 28642 respectively) soliciting information and comments from the public as to whether regulatory action relating to the purchase of annuity contracts was necessary and if so, what form such action should take.

After receiving over thirty letters in response, the Department reviewed the comments and, after extensive deliberation, the Department has determined that no regulatory action should be taken at this time to amend the minimum standards under the regulation at 29 CFR 2510.3–3(d)(2)(ii). More generally, the Department has decided not to promulgate any regulation limiting the circumstances under which the purchase of an annuity will be considered a full distribution of benefits for a participant or beneficiary such that the plan's and the employer's obligations to pay benefits have been served.

The following interpretive bulletin concerns solely the fiduciary standard and is published in addition to and independent of the regulatory minimum standard at 29 CFR 2510.3–3(d)(2)(ii).

The Interpretive Bulletin

The interpretive bulletin explains that, when choosing an annuity provider for purposes of a benefit distribution, whether for purposes of separation or retirement of a participant or upon termination of a plan, compliance with ERISA's fiduciary rules requires, at a minimum, that plan fiduciaries conduct an objective, thorough and analytical search for the purpose of identifying and selecting providers from which to purchase annuities. In conducting such a search, a fiduciary must evaluate a potential annuity provider's claims-paying ability and creditworthiness because the participants and beneficiaries whose entitlement to benefits will be transferred to the annuity provider have a paramount interest in the ability of the provider to make those payments. As a result, the interpretive bulletin states that a plan fiduciary choosing an annuity provider for the purpose of making a benefit distribution must take steps calculated to obtain the safest annuity available, unless under the circumstances, it would be in the interests of the plan participants and beneficiaries to do otherwise.5 The Department recognizes that, in many circumstances likely to arise under existing law, the interest of the plan participants and beneficiaries may require the selecting fiduciary to consider the cost of the annuity (to the extent that the cost is borne by the participants and beneficiaries) in addition to the annuity provider's

claims-paying ability.⁶ Cost consideration may not, however, justify purchase of an unsafe annuity.

The Interpretive bulletin also explains that an annuity provider's claims-paying ability and creditworthiness should be evaluated on the basis of a number of factors. Although ratings provided by insurance rating services may be a useful factor in evaluating a potential annuity provider, reliance solely on such ratings would not be sufficient to meet the requirement of a thorough and analytical search for an appropriate annuity provider.

List of Subjects in 29 CFR Part 2509

Employee benefit plans, Pensions.

For the reasons set forth in the preamble, Part 2509 of Title 29 of the Code of Federal Regulations is amended as follows:

PART 2509—INTERPRETIVE BULLETINS RELATING TO THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974

1. The authority citation for Part 2509 continues to read as follows:

Authority: 29 U.S.C. 1135. Section 2509.75–1 is also issued under 29 U.S.C. 1114. Sections 2509.75–10 and 2509.75–2 are also issued under 29 U.S.C. 1052, 1053, 1054. Secretary of Labor's Order No. 1–87 (52 FR 13139).

2. Part 2509 is amended by adding a new § 2509.95–1 to read as follows:

§ 2509.95–1 Interpretive Bulletin relating to the fiduciary standard under ERISA when selecting an annuity provider.

(a) Scope. This Interpretive Bulletin provides guidance concerning certain fiduciary standards under part 4 of title I of the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. 1104–1114, applicable to the selection of annuity providers for the purpose of pension plan benefit distributions where the plan intends to transfer liability for benefits to the annuity provider.

(b) In General. Generally, when a pension plan purchases an annuity from an insurer as a distribution of benefits, it is intended that the plan's liability for such benefits is transferred to the annuity provider. The Department's regulation defining the term "participant covered under the plan" for certain purposes under title I of ERISA recognizes that such a transfer occurs

⁴The Pension Annuitant's Protection Act of 1994, Pub. L. No. 103–401, 108 Stat. 4172 (1994) amended section 502(a) of ERISA to clarify the standing of pension annuitants to bring actions for fiduciary breaches that occurred. In addition, the Act specifies that a court may order appropriate relief to assure the annuitant's receipt of the amounts provided or to be provided by the annuity, plus reasonable prejudgment interest. The amendments made by the Act apply to any legal proceeding pending, or brought, on or after May 31, 1993.

⁵ This standard does not apply to the purchase of annuities for plan investment purposes. As with any other ordinary investment decision, ERISA's fiduciary duty of prudence requires that the risk attendant to such products, in the context of the plan's investment portfolio, and its funding, liquidity and diversification needs, must be weighed against the promised return. Thus, fiduciaries may select such investments that involve greater risks, but that also provide an expected investment return that is commensurate with that greater risk. In this regard, the Departu ment notes that in an investment contract with an annuity option, the standard described herein, while not applicable to the decision to invest in the investment product, nonetheless applies to the fiduciary's decision to exercise the annuity option.

⁶ Under IRC § 4980, an excise tax of up to 50 percent may be imposed on the amount of any employer reversion from a qualified plan unless the employer establishes and maintains a qualified replacement plan to which assets are transferred, or provides certain benefit increases for participants.